S. HRG. 114–8

REGULATORY RELIEF FOR COMMUNITY BANKS AND CREDIT UNIONS

HEARING

BEFORE THE

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

ONE HUNDRED FOURTEENTH CONGRESS

FIRST SESSION

ON

EXAMINING POTENTIAL CHANGES TO THE CURRENT REGULATORY REGIME AND THE IMPACT ON COMMUNITY BANKS AND CREDIT UNIONS

FEBRUARY 12, 2015

Printed for the use of the Committee on Banking, Housing, and Urban Affairs

Available at: http://www.fdsys.gov/

U.S. GOVERNMENT PUBLISHING OFFICE

94–014 PDF WASHINGTON : 2016

For sale by the Superintendent of Documents, U.S. Government Publishing Office
Internet: bookstore.gpo.gov Phone: toll free (866) 512–1800; DC area (202) 512–1800
Fax: (202) 512–2104 Mail: Stop IDCC, Washington, DC 20402–0001

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS

RICHARD C. SHELBY, Alabama, *Chairman*

MICHAEL CRAPO, Idaho	SHERROD BROWN, Ohio
BOB CORKER, Tennessee	JACK REED, Rhode Island
DAVID VITTER, Louisiana	CHARLES E. SCHUMER, New York
PATRICK J. TOOMEY, Pennsylvania	ROBERT MENENDEZ, New Jersey
MARK KIRK, Illinois	JON TESTER, Montana
DEAN HELLER, Nevada	MARK R. WARNER, Virginia
TIM SCOTT, South Carolina	JEFF MERKLEY, Oregon
BEN SASSE, Nebraska	ELIZABETH WARREN, Massachusetts
TOM COTTON, Arkansas	HEIDI HEITKAMP, North Dakota
MIKE ROUNDS, South Dakota	JOE DONNELLY, Indiana
JERRY MORAN, Kansas	

WILLIAM D. DUHNKE III, *Staff Director and Counsel*
MARK POWDEN, *Democratic Staff Director*

JELENA MCWILLIAMS, *Chief Counsel*
BETH ZORC, *Senior Counsel*
JACK DUNN III, *Professional Staff Member*

LAURA SWANSON, *Democratic Deputy Staff Director*
GRAHAM STEELE, *Democratic Chief Counsel*
JEANETTE QUICK, *Democratic Senior Counsel*
ERIN BARRY FUHER, *Democratic Professional Staff Member*
PHIL RUDD, *Democratic Legislative Assistant*

DAWN RATLIFF, *Chief Clerk*
TROY CORNELL, *Hearing Clerk*
SHELVIN SIMMONS, *IT Director*
JIM CROWELL, *Editor*

C O N T E N T S

THURSDAY, FEBRUARY 12, 2015

WITNESSES

Additional Material Supplied for the Record

REGULATORY RELIEF FOR COMMUNITY BANKS AND CREDIT UNIONS

THURSDAY, FEBRUARY 12, 2015

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, DC.

The Committee met at 10 a.m., in room SD–538, Dirksen Senate Office Building, Hon. Richard Shelby, Chairman of the Committee, presiding.

OPENING STATEMENT OF CHAIRMAN RICHARD C. SHELBY

Chairman SHELBY. The Committee will come to order.

This week, the Banking Committee began an examination of potential changes to the current regulatory regime. On Tuesday, we heard from the regulators on some ways to mitigate the regulatory burden on community banks and credit unions. Today, we will hear from those who are subjected to that burden.

We have asked our witnesses today to share their recommendations to us on ways to provide regulatory relief for smaller financial institutions and how the regulators can improve their review of outdated, unnecessary, or unduly burdensome regulations to make it more comprehensive and meaningful to everybody.

As the hearing on Tuesday demonstrated, I believe there is some bipartisan support here between the Democrats and Republicans, understanding that something, something substantive must be done to relieve the regulatory burden on institutions that provide essential banking functions to communities all across this country.

I look forward to hearing from our witnesses and I also will continue to work with my Ranking Member, Senator Brown. Senator Brown.

STATEMENT OF SENATOR SHERROD BROWN

Senator BROWN. Thank you, Mr. Chairman, and thank you to the five witnesses that are joining us today. I appreciate that very much. I look forward to hearing from you.

At last September's meeting, a group of witnesses similar to today's discussed a variety of regulatory relief proposals. Before the end of last year, Congress passed, pretty much everybody on this Committee supported, and the President signed into law several of those proposals where there was bipartisan consensus. I spelled them out at Tuesday's hearing. I will not repeat that list today. I thank a number of the Members of the Committee—Senator Vitter, Senator Warner, others—that were very helpful as sponsors of

some of that legislation that showed we can, indeed, work together to improve the regulatory climate for financial institutions.

If we hope to find consensus on more regulatory relief proposals, especially for community banks and credit unions, we will need to engage in a process similar to the one that allowed these bills to make it across the finish line, consensus among agencies and industry and consumer groups, all of our witnesses earlier in the week and our witnesses today, and we were able to do that.

In my first hearing in 2011 as Chair of the Financial Institutions and Consumer Protection Subcommittee, Senator Corker and I heard from some of the same organizations that are testifying today before this Committee about the opportunities and challenges facing community banks. It is notable how far the regulators have come since then, in no small part because Members of this Committee have asked them to do more for small institutions. The regulators understand the concerns raised by community banks and credit unions. They made it clear in their testimony 2 days ago and in their actions over the past several months. They have responded by making or considering changes to the supervision and regulation of these institutions in a way that lessens regulatory burden while at the same time safeguarding safety and soundness and the consumer protections that are in place.

As this Committee begins a process to determine if there are actions Congress should take to provide additional regulatory relief to the smallest financial institutions, I believe we need to do several things. We need to better understand the impact of the regulators' efforts. We need to determine if there is more the regulators should do through the EGRPRA review or other means to reach a relieved regulatory burden. We need to vet the proposals being recommended at this week's hearings, and we need to build stakeholder consensus on these proposals.

The privacy notice bill which I mentioned on Tuesday has gone through this type of process. We know the CFPB has done all it can within its authority to address this concern of community banks and credit unions. The current proposal, reintroduced by Senators Moran and Heitkamp earlier this week, has broad bipartisan consensus, 75 cosponsors last year, and has been vetted. I believe the Committee, as I mentioned to the Chair earlier in the week, should take action on this.

Another bill, to allow privately insured credit unions to become members of the Federal Home Loan Bank System, which I introduced last Congress, has begun this process, as well. Senator Donnelly is working on that legislation this year.

We know that there are no additional actions FHFA can take, and I believe that stakeholders are open to changes to the bill to reflect concerns raised at the end of last year. This is a successful model for our consideration of other regulatory relief proposals. It does not mean we will agree with every idea that deserves action. I want to reiterate that I am not interested in moving proposals that will weaken or roll back Wall Street reform, or undermine safety and soundness, or roll back consumer protections.

But, I think we should act on the proposals upon which we all agree, after fair consideration, those proposals that will make a difference for the smallest institutions. That is how this Committee

has worked in the past under Chairs of both parties and we are hopeful that is how the Committee—and have every reason to expect Senator Shelby and me to be able to work together and do the same thing.

Chairman SHELBY. Thank you, Senator.

I would like to remind my colleagues here that the record here will be open for the next 7 days for any additional statements and any other materials that you might want to submit to our witnesses, and I thank the witnesses for being here today.

Dan Blanton is the Chief Executive Officer for the Georgia Bank and Trust and the Chairman-Elect of the American Bankers Association.

Mr. Wally Murray is the President and Chief Executive Officer for the Greater Nevada Credit Union and is testifying on behalf of the Credit Union National Association.

John Buhrmaster is the President of the First National Bank of Scotia and the Chairman of the Independent Community Bankers of America.

Mr. Ed Templeton is the President and CEO of SRP Federal Credit Union and is appearing on behalf of the National Association of Federal Credit Unions.

And, Mr. Michael D. Calhoun is the President of the Center for Responsible Lending.

I welcome all of you to the Committee. Your written statements will be included in the record and I wish you would sum up your basic statements as quickly—within 5 minutes where we can have a question and answer period with you.

We will start with you, Mr. Blanton.

STATEMENT OF R. DANIEL BLANTON, CHIEF EXECUTIVE OFFICER, GEORGIA BANK AND TRUST, AND CHAIRMAN-ELECT, AMERICAN BANKERS ASSOCIATION

Mr. BLANTON. Thank you, Chairman Shelby and Ranking Member Brown. My name is Dan Blanton. I am the Chief Executive Officer of the Southeastern Bank Financial Corporation and Georgia Bank and Trust in Augusta, Georgia, and I am also the Vice Chairman of the American Bankers Association. I appreciate the opportunity to be here today to discuss ABA's agenda for America's hometown banks and to convey how the growing volume of bank regulation, particularly for community banks, is hurting the ability of banks to meet the needs of consumers and communities.

Community banks are resilient. We have found ways to meet our customers' needs despite the ups and downs of the economy. This job has been made much more difficult by the avalanche of new rules, guidance, and seemingly ever-changing expectations of our regulators. It is this regulatory burden that often pushes small banks to sell to banks many times their size. In fact, today, there are 1,200 fewer community banks today than there were 5 years ago. This trend will continue unless some rational changes are made to provide relief to community banks.

Every bank in this country helps fuel job creation, economic growth, and prosperity. The credit cycle that banks facilitate is simple. Customers' deposits provide funds to make taxes—I mean, to make loans that allow customers to invest in their hometowns.

The profits generated by these investments flow bank into the banks as deposits, and the credit cycle repeats, creating jobs, tax revenue, wealthy individuals, and capital to expand businesses.

Regulation shapes the way banks do business and can help or hinder the smooth function of the credit cycle. Every bank regulator changes—every bank regulation change directly affects the cost of providing bank products and services to customers. Every small change can reduce credit availability, raise costs, or drive consolidation. Everyone who uses bank products and services is impacted by changes in bank regulation.

Congress must take steps to ensure that the banking industry has ability to facilitate jobs creation and economic growth through their credit cycle. When a bank disappears, everyone is affected.

We urge Congress to work together, Senate and House, to pass bipartisan legislation that will enhance the ability of community banks to serve our communities. In particular, Congress can take action to ensure credit flows to communities across the country by improving the access to home loans. The mortgage market touches the lives of nearly every American household. Banks help individual consumers achieve lifelong goals of ownership by giving them access to funds that they need.

It is painfully clear that new regulations requirements have constrained the mortgage lending and have made it particularly difficult for first-time home buyers to obtain a home loan. Over-regulation of the mortgage market has reduced credit availability to bank customers, raising the cost of services and limiting bank products. The result has been a housing market that still struggles to gain momentum.

Congress should ensure that loans held in portfolio are treated as qualified mortgages. The Dodd-Frank Act is very restrictive on its definition of ability to repay and this is having a detrimental impact on the market and consumers with their credit. We support legislation that would deem any loan made by a bank and held in that lender's portfolio as showing ability to repay and, therefore, compliant with the Qualified Mortgage Act. Loans held in portfolio by their very nature demonstrate the ability to repay. Simply put, banks would not be staying in business very long if they made and held loans on their books that cannot be repaid. This is a common sense approach that does not impose additional challenges on borrowers and lenders in the lending process.

In addition, Congress can help community institutions by expanding the number of banks eligible for the 18-month exam cycle for highly rated community banks; providing an independent appeals process for bank examination decisions; by providing flexibility in the definition of rural for qualified mortgage designation purposes; and establishing a review and reconciliation process that will prevent the duplication of rules and eliminate redundant rules; and requiring targeted rulemaking for regulations that focus on the purpose of the rule; removing arbitrary regulatory thresholds not corresponding to the bank's risk and business model; approving Senator Moran and Senator Heitkamp's legislation, S. 423, that eliminates redundant annual privacy notices; and eliminating unnecessary currency transaction report filings; providing greater ac-

countability for law enforcement's use of the Bank Secrecy Act data.

ABA stands ready to help Congress address these important issues, and thank you, and I would be happy to answer any questions that you may have.

Chairman SHELBY. Thank you, Mr. Blanton.

Mr. Murray.

STATEMENT OF WALLY MURRAY, PRESIDENT AND CHIEF EXECUTIVE OFFICER, GREATER NEVADA CREDIT UNION, ON BEHALF OF THE CREDIT UNION NATIONAL ASSOCIATION

Mr. MURRAY. Chairman Shelby, Ranking Member Brown, thank you for the invitation to testify today for the Credit Union National Association. I am Wally Murray, President and CEO of Greater Nevada Credit Union and Chairman of the Nevada Credit Union League.

As the economy recovers, America's credit union members continue to rely on their credit unions for safe and affordable financial services delivered by institutions that they own, and we continue to provide tremendous benefits in terms of lower interest rate loans and lower fee or no fee products and services. Because credit unions are actively fulfilling their mission, consumers benefit to the tune of $10 billion annually. Yet, there are multiple statutory and regulatory barriers that keep us from more fully serving our members and we want to work with the Committee to reduce them. Doing so will significantly improve the impact credit unions have on consumers and the communities we serve.

Since the beginning of the financial crisis, credit unions have been subjected to more than 190 regulatory changes from nearly three dozen Federal agencies totaling nearly 6,000 pages. These new rules, usually aimed at curtailing practices that we do not engage in, impact us because we have to analyze the rule and determine how to comply, change internal policies and controls, design and print new forms, retrain staff, update computer systems, and help our members understand the changes. This costs money and time, both of which would be far better spent serving our members.

Recently, a number of Senators asked about the cost of complying with these rules. Sharing this concern, I am pleased to announce that CUNA is embarking on a major study on the impact of the regulatory burden on credit unions, including its costs. We are engaging in this effort because we know it is important to Congress to understand the cost impact associated with compliance, and, frankly, we have been disappointed with the regulators' efforts to quantify the expense their rules impose on credit unions and our members. We hope to have that data to share with the Committee later this year.

In addition, Congress should strongly consider why small institutions are being required to comply with rules more appropriately suited for too-big-to-fail banks and abusers of consumers. Policy makers universally say credit unions and community banks did not solve the problem, but you would not know that based on the hundreds of rules to which we have been subjected since the crisis. If you truly believe we are not the problem, please work with us to

remove the barriers that keep us from serving our members, your constituents, even better.

My written testimony includes more than two dozen recommendations for statutory changes. A few examples are: The Federal Credit Union Act has not kept up with the rapidly developing financial services industry over the last 20 years. The time has come to modernize that Act. We urge Congress to look at credit union capital requirements, restore full business lending authority, streamline field of membership, and grant new powers. In addition, we ask that Congress promote a fair examination system by creating an independent ombudsman and appeals process.

We also encourage Congress to ensure the CFPB uses its exemption authority to a much greater extent than it has to date. Members of this Committee have acknowledged that the Bureau has such authority, but we believe it is not being used sufficiently. We ask Congress to clarify and strengthen these exemption instructions as they pertain to smaller depository institutions, like credit unions. If a new rule results in a credit union doing less to serve its members, that rule has failed. A perfect example for credit unions is the remittances rule.

We also look forward to the enactment of legislation modernizing privacy notification requirements so that consumers receive meaningful information about how their personal financial data is being handled.

My written testimony also includes two recommendations related to the Federal Home Loan Bank System. One would permit more credit unions to join the system. The other would extend the Community Financial Institution exemption to include credit unions.

Finally, we urge the Committee to actively engage in the debate over data security. Credit unions and their members are greatly impacted by the weak merchant data security practices that have allowed several large-scale breaches, including those at Target and Home Depot, which have adversely affected my credit union and our members. The negligence of those that do not protect their payment information costs us a lot of money and shakes the confidence of our members. These breaches would be significantly reduced if those that accept payments were subject to the same standards as those that provide cards. We implore the Committee to hold hearings and consider legislation that ensures all participants in the payment system follow the same securities standards.

Congress does a lot to remove barriers for credit unions and community banks. It has not gone unnoticed to us that this hearing is one of the first that this Committee has held this year. We are grateful for this and we are hopeful that it indicates the priority of these concerns for the Committee. We look forward to working with you and thank you for the opportunity to testify today.

Chairman SHELBY. Thank you.

Mr. Buhrmaster.

STATEMENT OF JOHN H. BUHRMASTER, PRESIDENT AND CEO, FIRST NATIONAL BANK OF SCOTIA, AND CHAIRMAN, INDEPENDENT COMMUNITY BANKERS OF AMERICA

Mr. BUHRMASTER. Chairman Shelby, Ranking Member Brown, and Members of the Committee, my name is John Buhrmaster and

I am President and CEO of First National Bank of Scotia, a $425 million asset bank in Scotia, New York. I am also Chairman of the Independent Community Bankers of America and testify today on behalf of more than 6,500 community banks nationwide. Thank you for convening today's hearing.

We are here today to discuss a fundamental question: What is at stake for the future of the American banking industry? Do we want a system with fewer but much larger banks, more systemic risk, less consumer choice, and commodified product offerings? Will we allow large expanses of rural and small town America to be deprived of access to essential banking services? This Congress provides a unique opportunity to reflect on this troublesome but very real scenario and to enact legislation that will help reverse a dangerous trend.

Meaningful regulatory relief is needed to preserve the economic value community banks bring to our Nation. America is built on community bank credit, yet the rich tradition of community banking is at risk today because of regulatory overkill grossly out of proportion to any systemic or consumer risk posed by community banks.

A community bank is not a mega-bank on a small scale. The key characteristics of a community bank are a simple capital structure and business model, traditional products and services, and most importantly, a community-oriented character. It is a time-tested business model that built this country and has worked for generations.

The fundamental policy error of recent years has been applying monolithic regulatory mandates to community banks. Community banks deserve tiered regulation proportionate with their size and risk profile. Such relief is needed in the near term, not medium term or the long term. I urge this Committee not to let this opportunity slip.

ICBA's Plan for Prosperity is a robust regulatory relief agenda with nearly 40 legislative recommendations that will allow Main Street to prosper. Each provision of the plan was crafted to preserve and strengthen consumer protection and safety and soundness. A copy is attached to my written statement.

But, before describing it, I would like to thank the Members of this Committee for their leadership in the adoption of H.R. 3329 at the end of last Congress, which doubled the qualifying asset threshold under the Small Bank Holding Company Policy Statement. This Congress, you have already passed legislation to ensure community bank representation on the Federal Reserve Board of Governors. Both of these provisions are now law. On behalf of my bank and all community banks, thank you. These are steps in the right direction, but much more can and much more must be done.

ICBA's Plan for Prosperity is organized around three broad pillars. The first pillar is mortgage lending. Every aspect of mortgage lending is subject to new, complex, and expensive regulations that are upending the economics of this line of business. Our recommendations include qualified mortgage status for community bank mortgage loans held in portfolio and other critical provisions.

The second pillar of the plan is improved access to capital to sustain community bank independence. Our recommendations include

an exemption from Basel III, which was intended to apply only to large internationally active banks; relief from the costly mandates of S–Ox 404(b); and reform of Regulation D to ease investment in privately owned community banks.

The third pillar of the plan is reform of bank oversight and examination to better target the true sources of risk. Our recommendations include streamlining the quarterly call report and an extended exam cycle for highly rated banks, and reform of the bank exam appeals process to improve accountability.

The Senate bill from last Congress that best represented the scope of the Plan for Prosperity was the CLEAR Relief Act sponsored by Senators Moran, Tester, and Kirk. With more than 40 bipartisan cosponsors, the bill was a set of consensus solutions to ensure continued access to credit and other banking services. We are grateful to the Members of this Committee who supported the CLEAR Act. This Congress, we look forward to a new CLEAR Act with even more robust, yet sensible, community bank relief.

Last Congress, over 20 bills were introduced in the House and the Senate embodying Plan for Prosperity provisions. Chairman Shelby introduced a bill to require cost-benefit analysis of proposed rules. Senators Moran and Heitkamp have reintroduced a bill to provide relief from privacy notices. Six bills passed the House and many others passed the Financial Services Committee. These bills, most of which enjoyed strong bipartisan support, have set the stage for action in this Congress.

We strongly encourage this Committee to complete the work that was begun in the last Congress and enact meaningful regulatory relief for community banks. We look forward to working with this Committee to craft urgently needed legislative solutions.

Thank you again for the opportunity to testify today and I look forward to your questions.

Chairman SHELBY. Mr. Templeton.

STATEMENT OF ED TEMPLETON, PRESIDENT AND CEO, SRP FEDERAL CREDIT UNION, AND CHAIRMAN, NATIONAL ASSOCIATION OF FEDERAL CREDIT UNIONS

Mr. TEMPLETON. Good morning, Chairman Shelby, Ranking Member Brown, Members of the Committee. My name is Ed Templeton. I am testifying today on behalf of NAFCU, where I serve as the Chairman of the Board. I currently am President and CEO of SRP Federal Credit Union headquartered in North Augusta, South Carolina. The entire credit union community appreciates the opportunity to come before you today.

Credit unions have always focused on their members. However, the increasing complexity of regulation is taking a toll on the industry. The impact of the growing compliance burden is evident as the number of credit unions continues to decline. Since the second quarter of 2010, we have lost nearly 1,100 credit unions, 96 percent of which were below $100 million in assets. Many institutions simply cannot keep up with the new regulatory tide and have had to merge out of business or be taken over. Credit unions need regulatory relief, both from Congress and from the regulators, including the NCUA and the CFPB.

At SRP, our compliance costs have more than doubled since 2009, and we are actually adding another compliance officer in 2015 just to keep up. That is not getting ahead, that is just to keep up. Many credit unions find themselves in similar situations. A recent NAFCU survey found that 70 percent of respondents have noncompliance staff working on compliance issues, which takes time away from the mission of serving the members. Focusing on complying with unnecessary regulations keeps credit unions from fulfilling our core mission of providing our members with provident credit and other financial services.

My written testimony outlines NAFCU's updated five-point plan for credit union regulatory relief as well as our new top ten list of regulations that need to be amended or eliminated.

One of the greatest challenges the credit unions face today is the disconnect between the regulatory agency in Washington and the real world that credit unions and community banks operate in. While regulators have taken some small steps toward relief, too often, arbitrary thresholds do not actually consider the risk or complexities of institutions. Regulation of the system should match the risk to the system.

One example of a burdensome regulation where costs will outweigh the benefits is the NCUA's new risk-based capital proposal. The new proposal is a significant improvement over the initial proposal, but the problem with the regulation remains. The proposed rule is extremely costly and NCUA has not demonstrated why it needs a broad-brush regulation. Despite NCUA's estimate that a relatively small number of credit unions will be downgraded with its risk-based capital proposal, the rule would force most credit unions to hold millions of dollars of additional reserves just to achieve the same capital levels we currently maintain. These funds could otherwise be used to make loans to consumers, to small businesses, or aid in our Nation's economic recovery.

We also believe there are serious legal questions concerning the ability of NCUA to finalize the proposal as written. Ultimately, we believe legislative changes are required to bring about a comprehensive capital reform action allowing credit unions access to supplemental capital.

Next, NAFCU believes the field of membership rules for credit unions should be modernized on both the legislative and the regulatory fronts. NAFCU believes that reasonable improvements to current field of membership restrictions include streamlining the charter changing process, revising the population limits in NCUA's field of membership rules, and making statutory changes to allow all credit unions to add underserved communities to their working groups.

Cost and time burden estimates issued by regulators are often grossly understated. We believe Congress should require periodic reviews of actual regulatory burdens of finalized rules and ensure agencies remove or amend those rules that vastly underestimated the compliance burden. At SRP, we spend approximately 116 man hours to fill out one NCUA call report. NCUA's 2014 submission to the OMB estimated the time to do that at 6.6 hours. Something does not add up, 116 versus 6.6. There is a disconnect someplace.

All regulations must meet the test of whether the benefits outweigh the costs. We always need to have the end game in mind and make sure the regulation matches the true risk. There are a number of additional steps outlined in my written statement, both for Congress and the regulators, to provide relief.

In conclusion, the growing regulatory burden on credit unions is the top challenge facing our industry today. It must be addressed in order for credit unions to survive and meet the mission of serving their members' needs. We urge Congress to enact regulatory relief and hold regulators accountable to do the same.

We thank you for the opportunity to share our thoughts today with you and I welcome any questions you may have.

Chairman SHELBY. Thank you, Mr. Templeton.

Mr. Calhoun.

STATEMENT OF MICHAEL D. CALHOUN, PRESIDENT, CENTER FOR RESPONSIBLE LENDING

Mr. CALHOUN. Chairman Shelby, Ranking Member Brown, and Members of the Committee, today's hearing addresses the question of how we protect and promote critical community financial institutions while preserving consumer financial protections that are essential for the growth and integrity of our economy.

The Center for Responsible Lending is the policy affiliate of Self-Help, a community financial institution with over 30 years' experience providing banking services that help small businesses and families succeed. We have provided over $6 billion of financing for small businesses, home loans, and today have tens of thousands of families that depend upon us for deposit accounts, credit cards, home loans, and other basic financial products.

Before joining CRL, I spent a large part of my career working in those lending programs, and I also served as General Counsel dealing day to day with compliance issues. So, we know well the different business model and activities of traditional community financial institutions. The key is how to advance that effort.

Four principles apply. First, we must protect the integrity and fairness of our financial markets. Not only were community banks not the cause of the financial crisis, they were among the most severely impacted victims. While they did not offer the risky home loans that drove the crisis, the resulting recession stressed those banks and we lost nearly 500 of them in the ensuing years, and that occurred before Dodd-Frank rules went into effect. One of the most important advances in consumer regulation is, for the first time, nonbanks are now required to follow basic rules that banks have followed for so long. In providing relief to community institutions, we must continue those protections.

Second, relief must be directed to traditional community financial institutions. Many of the proposals that have been made would primarily or solely benefit larger institutions. Of course, there should never be unnecessary regulations for institutions of any size. But, where exceptions to otherwise effective provisions are being made to accommodate special business model community banks, they should be carefully targeted.

Overly broad provisions undercut basic protections, and also, they dilute the benefit of the provision to community banks. At

their worst, they create exemptions for nondepository entities, including the very players that pushed reckless lending in the past. For example, several of the mortgage proposals would apply to lightly supervised nonbanks and open the door again to reckless lending.

Focusing on traditional community banks also means focusing on the community lending model. Some of the proposals include exemptions up to $50 billion. Institutions in this category have very different business models from traditional community banks. They include American Express Bank, E*Trade Bank, GE Bank, and Morgan Stanley Bank. While those institutions provide important financial services, their markets and activities have little in common with traditional community financial institutions.

Third, overly broad exceptions undercut basic protections. We saw this with the bipartisan Military Lending Act, which protects service members from predatory loans. The original rules had several exemptions, and payday lenders and others learned quickly how to restructure their business to exploit them. As a result, the rules failed and our military bases today are still encircled with lenders targeting 400 percent loans at our troops. Congress has directed DOD to go back and rewrite those rules, which they are doing in this time. Fortunately, many of the agencies, as we heard earlier this week, are addressing how to preserve the community bank model and providing relief there. Most recently, the CFPB provided substantial revisions to the mortgage rules addressed to community banks.

Fourth, we must distinguish between community financial institution regulatory relief and proposed structural changes, such as to the CFPB. Those changes pose the greatest threat to basic financial protections. They also undercut efforts to deliver relief to the community banks. For example, we saw in the buildup to the housing crisis the budget process was used to hamstring oversight that would have countered the uncontrolled lending. When HUD tried to put restrictions on risky mortgages and when there were efforts to rein in the GSEs' excessive portfolios, both of those efforts were blocked with budget provisions. Similarly, structural changes such as commission undercut effective oversight. That is why the Senate in 2008 by a broad bipartisan vote explicitly required independent funding and a single director for the new regulator of the GSEs.

In conclusion, thank you for the opportunity to testify today. We look forward to working with the Committee, the other community financial institutions, and regulators in advancing the role and growth of community banking.

Chairman SHELBY. Thank you, Mr. Calhoun.

Mr. Blanton, arbitrary thresholds—in your testimony, you recommend removing arbitrary asset thresholds for certain regulations. If you were to remove arbitrary asset thresholds, what would you use instead?

Mr. BLANTON. Yes, I would propose a risk-based model that looks at the banks' risk profile that they are taking and set guidance based on that. In my State, Georgia, which has had a pretty tough economy, we have lost 87 banks. All of these banks, when you looked at their risk profile, were very highly leveraged in certain areas, but all of them would have been under a threshold. So, the

threshold, to me, does not really properly identify the type of business model these banks are in.

Chairman SHELBY. I think people know I am a strong believer in empirical analysis when it comes to regulations. If a regulation's cost outweighs its benefits, I believe it should be thrown out, or never brought forth. On Tuesday, we heard here from the Federal Reserve that it is easy to measure regulatory cost basis. Mr. Templeton, have the regulators done a good job analyzing costs and benefits?

Mr. TEMPLETON. Sir, the example I gave, I think, in my verbal testimony speaks somewhat to that. In our shop, it takes north of 100 hours just to do the call report. NCUA estimated that it is 6.6. If they use that type of data to do the whole industry, you can see the magnitude of the misrepresentation of the cost. That is a good example, sir.

Chairman SHELBY. In the area of *de novo* bank charters, Mr. Buhrmaster, it is my understanding that only two *de novo* Federal banking charters have been approved since 1909. On Tuesday, we heard from the FDIC that this is due to, quote, "the economic cycle," not, quote, "legislative barriers or even regulatory barriers." Are regulatory barriers, Mr. Buhrmaster, standing in the way of new banks being formed?

Mr. BUHRMASTER. Well, we have seen some economic recovery in parts of the country——

Chairman SHELBY. Uh-huh.

Mr. BUHRMASTER.——much of the country. So, clearly, I do not believe it is part of the economics of it. What I do believe—or, the national economics. What I do believe is I have got a stack here—I asked my compliance officer to show me all the regulations she has had to look at, that is guidances, changes, and so forth. I had to print it in small print so I could actually not over-exceed the weight limit on the plane. But, this is 7 years' of changes these folks have had to do. Now, a *de novo* for the first 7 years is going to be subject to all of this. It is a crushing burden on a new business, and, frankly, they are small businesses. Would you open a small business if you had to deal with this amount of regulatory burden?

Chairman SHELBY. It would not happen, would it?

Mr. BUHRMASTER. It would not happen.

Chairman SHELBY. I will direct this question to the credit union. A lot of us are concerned when regulations limit choices, increase costs for consumers, or perhaps cause institutions to stop offering products altogether. Mr. Murray, have any regulations increased the cost of products or services that you offer your members or caused you to stop offering them altogether?

Mr. MURRAY. A great example of that in our shop is the remittances rule that was put forth by CFPB. That forced us to raise the prices of that service for our members after we first had to make a choice about whether or not to continue with that service at all. That is a choice that many credit unions, they opted out of that service simply because of the cost of that regulation and found it too burdensome to continue to offer. Again, the cost-benefit just was not—it did not stack up. So, that is a great example of one

where we have had to raise our price by 10 percent or more just to stay up with that——

Chairman SHELBY. That is where you need some relief, is it not?

Mr. MURRAY. We would love some relief in that area.

Chairman SHELBY. Risk-based capital proposal—last month, the National Credit Union Administration issued a revised proposal regarding the capital standards for credit unions. Mr. Templeton and Mr. Murray, what are your views on the revised proposal, and has the National Credit Union Administration conducted a sufficient cost-benefit analysis?

Mr. TEMPLETON. First, I would say that the current proposal is a significant improvement from the first proposal, so I would applaud NCUA for moving in the right direction. But, I think the real question still remains, is this a regulation that has a purpose for being in existence?

When we take the regulation as proposed and roll it back over the last 9 years—and the calculations are not crystal clear, you have to make a few assumptions, so let me just be clear on that—but, when we take the regulation, apply it retrospectively, 95 percent of the credit unions that would have been problematic under the regulation came through the last 9 years and are healthy and alive today. Very few credit unions would not have made it through. What the proposal would have done is it would have made it extremely hard or intensified the pressure on all credit unions to raise additional capital that would have been called for under the regulation.

Now, does that mean it is not necessary? I think it is a good indication it is not necessary and it has not been thoroughly analyzed, and particularly with the benefit of looking back. We can look back right now and really see if, in a hard time, this rule would make a difference. So, that is where I think we are on that, sir.

Chairman SHELBY. Thank you.

Senator Brown.

Senator BROWN. Thank you, Mr. Chairman.

I want to dig a little more deeply on the issue of costs and benefits of these regulations. That seems to be the primary purpose of this hearing, to discuss that. Mr. Calhoun, I would like to ask you, we heard in today's—I am sorry, in Tuesday's hearing that the regulators already conduct significant impact analysis of their rules, both during the rulemaking stage as well as retrospectively, in addition to the EGRPRA rule. Several agencies noted on Tuesday that they conduct ongoing reviews of their rules more frequently and voluntarily. The regulator of credit unions, the Consumer Bureau, they do those without being required to by Federal law. Witnesses pointed to the inherent difficulty in assessing the benefits of a rule, especially sort of the societal-wide benefits, since preventing another financial crisis or ensuring that consumers have protections before subject to predatory lending may not be easily quantifiable beforehand.

Several recent bills offered by some Members of this Committee and others have proposed that we should require agencies to undertake more cost-benefit analysis as they proceed. Tell us your opinion of these bills, many of which have broad applications across more than just financial services through the Government, but par-

ticularly impact financial regulators. Give us your thoughts about some of these requirements.

Mr. CALHOUN. Well, certainly, agencies must consider the burden of their regulations, both when they are considering them in the first place, and they need to go back and look at them again. I mean, for example, the CFPB has a requirement that they have to go back and reevaluate every regulation after a 5-year period in addition to their evaluation at the outset.

But, many of these cost-benefit analyses are very challenging, and let me just give one example. A proposal which most of the members here strongly supported was the reform of our credit card market, but at the time that that was proposed—it initially was proposed by the Federal Reserve using their rulemaking authority—there were predictions from industry that it would not only destroy the credit card market, but pose systemic risks to the whole banking system because of the stress on the credit card banks. And, if the agency had to cost that out, I mean, those are very difficult projections, and understandably, and we have seen this ourselves, when you have to comply with the regulations, you look at them from a different viewpoint, often, than when you are writing them.

But, if you impose a burden like that, particularly with the ability to block all regulations by legal challenges, I think we throw the baby out with the bath water there and we end up with just gumming up the whole system. Again, clearly, the burden has to be assessed on initial and ongoing basis, but these proposals, I think, again, would throw the baby out with the bath water.

Senator BROWN. Thank you.

Give me a brief answer on this. Are costs easier to—costs to the banks and the credit unions, and then Wall Street, too—are costs easier to quantify than benefits?

Mr. CALHOUN. They are, but they are often exaggerated. If you look in the consumer product world, another example was when it was proposed that lawnmowers have a cutoff device, it was projected by industry that that would add $500 or so to the cost of every lawnmower. Well, now you can still go buy a lawnmower with a cutoff device for under $200 at Walmart. I mean, it is very hard to know—there is as much art as science in projecting both the costs and even more so the benefits.

Senator BROWN. Let me pursue one more question——

Mr. CALHOUN. Yes.

Senator BROWN.——Mr. Chairman—Mr. Calhoun, on costs. Today and in Tuesday's hearing, several questions were asked about the increasing costs of compliance to community banks and credit unions after the passage of Dodd-Frank. What has been your experience with compliance costs?

Mr. CALHOUN. I think our experience, and we are a—we have Federal and State credit union charters and go through the call reports and everything that everybody else gets to have the fun with—a lot of that came as a natural reaction to the financial crisis, that you did have lots of institutions failing, again, mainly due to the macro effects, but that led regulators to more carefully scrutinize all financial institutions. And, so, that has been, from our view, the biggest driver of it.

We do think there needs to be review and concern about overlapping regulations. We applauded the regulators, for example, for uniting the QM and QRM rule. That would have been a whole another layer of mortgage regulation, that I think the regulators heard the call to say, simplify that and make them the same. So, we think that we are getting some response from the regulators. Clearly, efforts like today help highlight these issues in a very beneficial way.

Senator BROWN. Thank you, Mr. Chairman.

Chairman SHELBY. Senator Corker.

Senator CORKER. Thank you, Mr. Chairman, and thank you for having this hearing, you and the Ranking Member, and I want to thank all of you for your testimony.

I am going to ask all of my questions to Mr. Blanton, but I just want to say this. I have seen nothing like Dodd-Frank to alleviate the tensions between the credit unions and the banks——

[Laughter.]

Senator CORKER.——and, I will say, it is a welcome reprieve for all of us who have had to have to deal with that tension.

But, to Mr. Blanton, as we look at encouraging private capital back into the mortgage market, it seems one of the easiest things we can do is deem loans held in a lender's portfolio as compliant with the QM standard for the purpose of a borrower's ability to pay. I understand that the CFPB partially addressed this issue through its Notice of Proposed Rulemaking. Last Congress, legislation was introduced in the House, H.R. 2673, that would provide broader and more permanent relief for any depository institutions that make loans and hold them on portfolio.

Why is this relief provided—why is the relief provided by the CFPB insufficient, and why would the legislation introduced last Congress be such an improvement, and what do you say to those who suggest relief like this would lead to the proliferation of some of the predatory products we saw leading up to the crisis?

Mr. BLANTON. Thank you. Survival is a real driver for cooperation, so——

[Laughter.]

Mr. BLANTON. With the QM rule—you know, my whole career, I have been making a loan to where the father would call me and say, "My son is getting married. He and his wife really do not qualify, but we have got to get them in a house." I would say, "Fine. We will take care of it." I have made hundreds of those loans. Now, under the definition now, I know from day one they do not qualify. I cannot put my bank in the position of making that loan where I have put more people in fresh and new homes, new couples for that scenario—and that is what community banks do, is we have this relationship with these borrowers, and we have the father call us and say, "Please help my son or my daughter." With this definition now, if I cannot deem that QM from day one and put it on my books, I have now put my institution at risk. And, so, these are the things that we need to see legislation passed to allow us to continue to make this relationship loan that we have always made and help this young couple into a house.

Senator CORKER. And, I was not actually going to do this, but Mr. Calhoun, if you could briefly respond. It seems to me that that

is a legitimate thing, that the three Cs—character, character, and knowing the people you are dealing with—has been a fundamental part of our banking industry for years. Would you have any opposition to that type of thing?

Mr. CALHOUN. So, we have very strongly supported the expansion of QM status for community bank loans on portfolio, but it is a different business model. I would note, even in the crisis, WaMu and Wachovia, for example, two institutions that both went under largely due to unsustainable loans on their portfolio, and when you are looking at a refinancing, it is the borrower's equity in the house—and the majority of loans still today are refinances—it is the equity in the house that is providing the cover.

But, we are strong supporters, again, for community financial institutions. His lending model is very different from a large bank where it is much more routinized and impersonal, so——

Senator CORKER. So I have a consensus on this point?

Mr. CALHOUN. I think there is a large amount of consensus on this point.

Senator CORKER. My second question. If you think back to the terms of the underlying reasons behind the Volcker Rule, I think you would be hard pressed to find anyone that thought it was needed because of the activities of community banks. Yet, according to the letter of the law, banks must be in compliance. On Tuesday, Mr. Bland of the OCC said that the compliance effort to make that determination seems costly compared to the actual activities that smaller banks have. What does it mean for smaller banks that never engaged in proprietary lending but still need to be in compliance for the Volcker Rule?

Mr. BLANTON. Well, we first saw we do have to do an analysis to even determine where that qualifies, and most community banks, the only part that they are involved in is maybe the deposit accounts of local municipalities and all. And, so, for us, it is just a very expensive process to make that determination and then have to deal with that.

Senator CORKER. And, Mr. Calhoun, briefly, do you have any issue with that type of proposal?

Mr. CALHOUN. So, the Volcker Rule requires community banks to still document that they are not covered. There seems to be room there for relief to make that certainly easier and less burdensome than it is now, again, for community banks.

Senator CORKER. Yes. Well, it seems like we are making a lot of progress here.

[Laughter.]

Senator CORKER. I would say that—my last point, and I know there will not be time to answer unless the Chairman gives me a second, but the Bipartisan Policy Center suggested creating a pilot program for a consolidated examination force for institutions subject to supervision by all three of the Federal prudential regulators. Such a program would force coordination between agencies and minimize the costs associated in examination for banks. It appears that the Federal Financial Institutions Examinations Council would provide the vehicle to run the pilot program. Just briefly, Mr. Blanton, do you think this is something that would be a good idea?

Mr. BLANTON. I think it is something that needs to be explored. I do not—I think more information needs to be looked at, but I think it certainly ought to be explored and might very well have good credibility to it.

Senator CORKER. Thank you all for being here and for what you do in your communities around the country. I do not know why we have two institutions separated by the Savannah River here at one place, but we are glad to have you.

[Laughter.]

Senator CORKER. Thank you very much.

Chairman SHELBY. Senator Menendez.

Senator MENENDEZ. Thank you, Mr. Chairman, and thank all the witnesses for their testimony.

You know, banking is a regulated industry, and with good reason. One need to look no further than the financial crisis, when millions of Americans lost their homes, jobs, and retirement savings, and businesses across the country had to close their doors and let their employees go, and taxpayers had to bail out some of the worst offenders just to prevent an even bigger meltdown. But, I also believe that regulation is not a one-size-fits-all exercise. A community bank or credit union that makes loans to small businesses and home buyers poses different risks and should be treated differently from an integrated mega-bank with multinational scope and sophisticated trading operations.

So, I am eager to work with my colleagues on both sides of the aisle on targeted consensus measures that help small institutions better serve their communities and compete in the marketplace and to reduce unnecessary burdens for institutions of any size. However, in the desire to do that—and I have often said that community banks were not the cause of our financial crisis in the preceding years—I would, however, caution that those who would seek to use regulatory relief for small institutions as a pretext for other goals, such as gutting important consumer protections or financial reforms, will face a challenge by many of us.

I believe that regulatory relief is compatible with protecting consumers, investors, and taxpayers, but I would have serious concerns about attempts to hijack the process and undermine these goals, for example, by creating overly broad carve-outs or imposing a rigged version of cost-benefit analysis that would block almost any regulatory action and invite frivolous legal challenges at taxpayers' expense.

So, I think that regulatory relief, at least as I envision it, to make and help community banks and credit unions and others be able to function effectively in the marketplace and help consumers is a shared bipartisan interest, but I hope it is not the opportunity in which some will look to slay the very provisions that ultimately have brought us further and further back away from the systemic risk that created not a systemic risk just for those institutions, but for the entire Nation. I do not want to relive that again. But, I do want to work with all of you to create greater abilities to be able to function and function effectively and, of course, with the appropriate oversight.

So, let me ask all of you, I have heard from some community banks in my State that when a dispute comes up in the context of

an examination, they do not always feel that there is a sufficient process available for fairly resolving the dispute. And, I would add that these are not cases where the bank is looking for an opportunity to challenge or appeal every decision that goes against them. They just want to know that the mechanism exists where their concerns can be fairly heard and appropriately responded to in a timely manner.

For any of the witnesses, to the extent that this has been an issue for you or your institution or members of your association, can you discuss what type of improvements you think can be made in that regard. For example, are there changes that you would make to the ombudsman's office of your respective regulators? Mr. Buhrmaster.

Mr. BUHRMASTER. Well, first, let me just respond to your first comments that if a proposal that we have before you to reduce regulatory burden affects safety and soundness or consumer protection, it goes against everything that the community bank is for, and that is not something we could support. So, please be assured that what we are asking for is to allow us to deliver better service to our consumers and to help promote entrepreneurship among small businesses.

So, that said, an examination process—I had an exam a couple of years ago where we had one examiner who really did not look at the entire packet of information he was given, and we received a warning on that information. We did not feel that was right. We felt the examiner did not do his job properly. We moved up the channel. Fortunately, we have—in our area, we had an examiner in charge of the regional office that listened and worked with us and worked through that issue.

But, as I travel the country talking to different community bankers across the Nation, it depends on what agency and it depends on your regional administrator or the food chain up on whether or not those type of things can get removed. I remember earlier in my career we had a similar issue. It ended up going to D.C. and we did not prevail. We did not go to the ombudsman, because, frankly, it is scary to report an individual examiner to an ombudsman. You just do not know. That guy is going to come back into your bank sometime.

So, I think there needs to be more transparency. In our Plan for Prosperity, we do have a proposal there that deals with this, and I would hope that this Committee would take a look at that proposal and enact some changes.

Mr. BLANTON. You know, I completely agree with John's comments. Our whole mission is to take care of our communities and protect them. We would never support any legislation that would in any way try and harm our borrowers or harm our businesses. I mean, that is what we do. We look after our communities.

As far as the proposal for an independent ombudsman or regulatory review process, as I cross the country, I have the same stories of people, one, that are scared to use the ombudsman within the existing agency. I understand that. They are paid by that agency. They work for that agency. And, there is a tendency to kind of shy away from using that. An independent agency would have the

ability to review, and you have a proper place to present your challenges to the exam.

Exams do vary all over, depending on the scope and the experience of the examiner. Our exam teams have been very well, and Georgia has had a lot of activity with our exams and, by and large, have been handled very well. But, there are—as any large agency throughout the country, there are different levels of expertise down through the ranks. And, so, I can see some real value in being able to have an independent place to be able to come and discuss the findings of an exam. So, we do support that.

Senator MENENDEZ. Thank you, Mr. Chairman.

Chairman SHELBY. Senator Crapo.

Senator CRAPO. Thank you very much, Mr. Chairman. I appreciate your holding these hearings. This is not the first time that you and I and this Committee have worked together to put together a package for reform of our regulatory system for financial institutions and I appreciate the focus on community banks and credit unions in this hearing.

The first thing I would like to do with the witnesses is—and I am not going to ask you to answer this question right now. I am going to ask you if you will please send me a written response to this question. But, the question is, can you identify some of your top priorities for the kinds of reforms that we need, the kinds of regulatory reform that this Committee should look at as we prepare for legislative or regulatory oversight. Do you think all of you could come up with a list of two or three or four or five, or I do not want to limit it, five or ten top reforms?

[Witnesses nodding.]

Senator CRAPO. I see everybody shaking their head in the affirmative. So, please, if you would, send those to the Committee.

Now, with some—and you can refine this list before you send it to the Committee. But, do you all have some ideas in your mind right now that came to your mind as I asked whether you had some top priorities? I would like to ask you, and you can probably answer these questions just by raising your hand, if it fits. Do some of those top priority reforms that you think the Committee should consider fall under CFPB jurisdiction?

[Witnesses raising hands.]

Senator CRAPO. Four of the five hands went up, Mr. Chairman.

Do some of them fall under Dodd-Frank rules and regulations?

[Witnesses raising hands.]

Senator CRAPO. I think all the hands went up on that.

Do some of them fall under money laundering legislation or regulation?

[Witnesses raising hands.]

Senator CRAPO. Five of the five hands went up.

The reason I am asking this question is because each of those categories that I just listed to you, I understand to be exempted by the EGRPRA process from our regulators from review. In the testimony before this Committee yesterday, the regulators told us that they were not looking at Dodd-Frank regulations in their EGRPRA review process. In the footnotes to the EGRPRA process that has now been started, it says, as the law says, that CFPB regulations are not—or, the CFPB is not required to participate in EGRPRA,

and money laundering provisions are not going to be considered, again, because the law does not require it.

So, my question to you is, if we are having the Federal agencies review the burden of regulations on the financial institutions and our effort there is to try to identify outdated, unnecessary, and unduly burdensome regulations, and each of you say that some of your top priorities fall in the very area that our regulators tell us is not going to be reviewed, do we need to reform the EGRPRA process? And, again, I would just like to see by raise of hand if you would agree with that.

[Witnesses raising hands.]

Senator CRAPO. I see three or four or five—in fact, maybe, I think, five hands went up.

I do believe that this Committee will not be limited by the restrictions that the regulators have claimed they are following with regard to the EGRPRA process. I have previously in hearings with the regulators encouraged them not to self-limit themselves in this review, and I, frankly, would encourage you in your comments and participation in that process to continue to bring up these kinds of issues, even though the agencies may tell you they will not listen to you, because I believe that this Committee is going to do its part through oversight to try to get those agencies, whether it is in the EGRPRA process or otherwise, to look at these issues.

Just from the testimony that we have had here today—the QM example has been brought up—I do not think that the agencies would have looked at QM under EGRPRA. The Volcker Rule has been brought up. I do not think the agencies will look at the Volcker Rule under EGRPRA, under their current approach to it.

And, so, my point is, I think that we have got to expand the focus of our Federal agencies who are looking at this issue. I appreciate again, Mr. Chairman, your willingness to have this broader review, and I hope that through the input received from those like our witnesses today, as well as from the oversight that this Committee provides, that we can help our Federal agencies to also—our regulatory agencies to also expand their view about how we should approach helping the community banks and the credit unions and other financial institutions in this country. Thank you.

Chairman SHELBY. Thank you, Senator Crapo.

Senator Donnelly.

Senator DONNELLY. Thank you, Mr. Chairman, and I want to thank all of you for being here.

I had the privilege of serving on the Financial Services Committee during some of the most difficult times over in the House of Representatives, and one of the things that was most heartbreaking was so many of our small businesses in Indiana having their credit lines ended because it was such a challenge for the banks, as well, at that time, and to see them not being able to get inventory lending, floor plan lending, all of those things that affected our small businesses. I wanted to make sure that we never had to do that again, and that is why we worked to ensure the safety and soundness of our financial system, and so that is, like, the cornerstone of everything we do.

But, then I sit with my community bankers and credit unions and they go, you know, number one, we were not the folks who did

it, and we all understand that. But, number two is, those are our goals, to make sure those businesses continue to be able to get those loans and the credit lines, but here are some things that we are now dealing with that have made it tougher for us to maybe not sell at the end of the year or to make it more challenging.

So, if you each had one or two things that when you look at, you go, hey, the safety and the soundness of the system will be protected, but this does not do anything but make our lives more difficult, if you could just give me one each——

Mr. BLANTON. Well, I mean, I go back to the mortgage process now. My bank does originate a quite good number of mortgages. In the process, where just a few years ago you would sit down with an originator and make an inquiry, you would just simply, you know, what is the mortgage market, what are the rates and all now, that is now an application, so, now I go through a very rigorous process of logging in this application, all this tracking, that just a few years ago was nothing but a polite conversation between an originator and a borrower. And, so, now I have got all this log I have got to do, all this tracking, and I have to do it in a zero-tolerance environment with humans involved. I am sorry. That is very difficult. We have the best intentions, but it just does not always translate when you get it onto paper.

And, the amount of work now that my mortgage department is doing tracking this, it has quadrupled, quote, our "applications." It has quadrupled not only that, you now have to send them a decline letter. Just because it is now considered an application, you have to send them a decline letter. They get a letter and go, they did not even apply as far as they were concerned. They were just doing an inquiry, just kind of what is going on, and seeing now you have declined me? And, so, they are insulted. I have sat here and given them a decline letter.

So, that is just one example with my bank of the amount of expense I have to do in a zero-tolerance environment, and there again, I say, that is really hard with humans.

Senator DONNELLY. Mr. Murray.

Mr. MURRAY. I would agree that the mortgage side is a big, big challenge. You know, when the QM rules came out and we started having to have the conversations internally about, OK, what kind of borrowers will not qualify for this, I mean, that is just kind of going back to the period that you were referring to, about when we were making decisions to save the institution at the detriment of consumers. We are having those same kind of conversations when it comes to QM.

So, we have taken a conservative approach. We have said we are not going to do any non-QM loans right now. We are going to take a wait and see and see how it all plays out. That is not the way to serve our communities effectively, and so I beseech you to look at that and understand the true impacts of that on the communities that it is affecting.

Senator DONNELLY. Sir.

Mr. BUHRMASTER. Yes. First of all, we never did a better business in small credit lines as we did when all those large banks were canceling our customers and they were coming in to us saying, "How do I get my inventory?" That year, we did a bang-up

business on small lines of credit, and we have kept those customers.

Things in the regulations that are harming small businesses, especially—that was the focus of your question, I believe—the equity in someone's home is the greatest source of capital for a startup business, and granting home equity loans or first lien mortgages on a house that someone wants to mortgage to put the money into their business has become so difficult because of the high-cost mortgage and the ability to repay part of the QM. If loans held in portfolio by community banks, by these institutions, were exempt from that rule, we would be able to provide more capital to businesses because we would not have to be restricted.

The hardest loan to make right now is to a small business, a self-employed individual. I had an individual, he wanted $30,000 on a first mortgage, and I only got the call after he had given up and gone and found money somewhere else. The guy had been with us for 20 years. He has done this a couple times before. We had to make him jump through hoops to provide us with all this documentation to prove he had the ability to repay, because our recognition of his character was not enough. That is what is harming businesses, QM.

And, then, the fact that on Basel III, we are losing the ability to—we are losing capital when we write a development loan. I want to help develop commercial properties, yet it costs me more in capital to do those loans now.

Senator DONNELLY. My time is up, but——

Mr. TEMPLETON. To carry that tide on down the table, QM is just really changing the whole atmosphere for the small lender in our marketplace. When QM first rolled out, we automatically got to the conclusion we were not going to do nonqualified because the risks were just too great. As we dug and dug and dug, we determined that we could not back away from that market, because if we did, it was going to be a substantial portion of our business.

But, what we did have to do is we had to lop off, for lack of a better phrase, the outliers, the people that were on the fringe that, up until then, we would take the risk on them, and up until then, our track record had been near perfect over 25 years. I think in 25 years, we lost maybe two times on a loan like that. The track record indicated those people are going to work with us because we work with them.

But now, all of a sudden, they have got a brand on the mortgage that says "nonqualified." It is a target in the event of any type of catastrophic event in that person's life, and the outlier presents just too much of a risk today, where 10 years ago, that was bread and butter to us. They loved us because we were able to do something for them that a person on the street called a loan shark or a finance company was willing to do for 35 or 40 or 50 percent and we would do it for 8 or 9 percent.

Senator DONNELLY. OK.

Mr. TEMPLETON. And, those days are gone now.

Senator DONNELLY. Thank you, Mr. Chairman.

Chairman SHELBY. Senator Scott.

Senator SCOTT. Thank you, Mr. Chairman, and thank you for providing the opportunity to have this conversation today. I think

it is a very important conversation and one I will continue along the lines of Senator Donnelly.

I will just tell you a very quick story. As a kid growing up in the insurance business, I had an opportunity to start a business, a small Allstate Insurance franchise with a 1990 240–SX with 253,000 miles. I went to a big bank and said, "This is my asset." They all—looking at your faces, they all laughed, too.

[Laughter.]

Senator SCOTT. I got used to that, very comfortable four or five banks into it. But, I went back to the bank where I had the longest relationship and shared my business plan and had a conversation and the banker said, "I can do something called a relationship loan, a character loan." I cannot imagine in the current environment—though you had nothing to do with the failure of our economy—that you would be in the position to take that risk, because if I understand the rules and the regulations fairly, that any unacceptable risk on your books brings attention in waves that would be disconcerting and challenging for you to overcome that threshold.

Is that an accurate statement, that today's environment would not allow you to provide a kid like me—a kid like me several years ago—an opportunity to move forward and starting my own business? Is that accurate, Mr. Buhrmaster?

Mr. BUHRMASTER. I believe that is accurate. I think that for someone starting—we have done State Farm loans. We have——

Senator SCOTT. Allstate.

Mr. BUHRMASTER. I am sorry, Allstate——

Senator SCOTT. Please. Please.

[Laughter.]

Mr. BUHRMASTER. OK.

Senator SCOTT. There are some things that cannot be allowed on the Banking Committee.

[Laughter.]

Mr. BUHRMASTER. I actually have an Allstate loan.

[Laughter.]

Mr. BUHRMASTER. I do believe in good hands. Let us just get this right. So, we have done Allstate, as well——

Senator SCOTT. Good.

Mr. BUHRMASTER. We have done those, too. You are passing generational businesses or you are picking up a new business——

Senator SCOTT. Absolutely.

Mr. BUHRMASTER.——and those are character loans. That is what our economy is based on. And, yes, we can do some of those. They are harder to do right now, much harder. But, again, it is that source of equity. What really puts the brakes on it right now is if you are using a home for any part of that financing of that project, it kills it. It is very difficult.

Senator SCOTT. Let me take that question—because you just created a segue into Mr. Blanton's earlier conversation about the QMs and the ability to create access to capital and/or to a home to folks that you have had a long-term relationship with not only the borrower, but their family. And, so, if you could put into context for us that actual process and how challenging it is today compared to speaking to how challenging it was. And, in the context of safety and soundness, could you and would you be able to create a nar-

rative that makes sense to your board of directors and to your institution but not to the regulators?

Mr. BLANTON. It is really hard to document to your regulators, but as far as safety and soundness, those loans that we can make and we keep on our books are some of the safest loans we make because we have that relationship with that family and have had it for generations.

I know a lot of my rural colleagues in Georgia, some of their prime loans may be five acres and a double-wide——

Senator SCOTT. Yes.

Mr. BLANTON.——and they have done it year after year after year. What the regulators do not seem to understand in that environment is if you force to where I cannot make that loan anymore and I cannot put it on my books, that family does not have the luxury of saying, "Well, we will just do without the money." They are going to get the money. They have no choice. So, now, where are they? Down the street at a much higher interest rate environment that is not constrained by all the constraints that we have because they had no choice. They had to generate $5,000 or $10,000 or whatever the amount was. Well, these people in a lot of cases are self-employed. Trying to fit them into an ability to repay definition is virtually impossible.

Senator SCOTT. Yes, very difficult. And, I will tell you, according to a Harvard Kennedy School working paper authored by Marshall Lux, one of the unintended consequences of Dodd-Frank is that community bank small business lending has declined by about 11 percent, and small business banks, a billion dollars or less in assets, their share of banking assets have also declined by 19 percent, as if too-big-to-fail is more likely today than it has been before the regulatory environment was created.

Let me just ask my final question, with my time running out, to Mr. Templeton. As you know, sir, I served for about 7 years on a credit union board, back when I had an afro. Let me just ask you a question, though. Looking at the current environment, what is the impact on your ability to loan? How many folks are you employing today who are involved in the regulatory responsibilities of the credit union versus the lending part of the credit union? And, what does that look like for the future of credit unions if what we have seen so far gets worse?

Mr. TEMPLETON. Today, we have two people employed full-time. We are in the process of adding a third person full-time. But, that is only the beginning of the compliance costs. Those are people who are dedicated 8 hours a day to doing nothing but compliance. Every time we have a new product, every time we have a feature change, we have to reach down into the functional departments and involve those people in the compliance aspects of how are we going to be compliant on this new modification. So, those numbers exponentially go up.

To maybe answer your question another way, the loan that you talked about that used to could be done in many local banks and credit unions was a 5-minute loan in many cases back then. Yeah. I know you. I have known you forever. I trust you. Let us get the paperwork done. Today, that loan may turn into 15 or 20 or 30 hours. That is a regulatory compliance burden. That is an overhead

cost that is not measured in all the assessments of the risk and reward.

If you talked to me today about that loan, I would say, well, let me get back to you. So, I go and I talk to the financial analyst and I say, what do you think? I go and talk to this person. I go and talk to that person. And, the process goes on and on and on.

Senator SCOTT. Thank you.

Mr. CALHOUN. And, if I may add, Senator, just to make sure it is clear for the record, the CFPB proposal, which I think most people here have supported and I know ICBA has praised, would allow unlimited portfolio loans for community banks to qualify for QM status. Another area where we can have clarification, we do a lot of small business lending. We can have more clarification that the QM standards should only apply to consumer loans and business loans are generally taken outside of that, but we can get more clarity on that, I think that would be a specific thing that could help.

Senator SCOTT. Thank you, sir. Thank you, Mr. Chairman.

Chairman SHELBY. Senator Heitkamp.

Senator HEITKAMP. Thank you, Mr. Chairman.

I grew up in a town of 90 people. You can imagine, my family had a relationship with a community bank. Whether it was financing a home that you could never get an appraisal on, right, because where are you going to find a comparable sale, right? Whether it was helping my father finance his business and cash-flow his business, or looking at a farm that needed a quick operating loan because of some tragedy.

I think the great irony of this is, in spite of all that relationship banking and that character banking that you do, you were not the institutions that failed because you were banking every day on the American people and your relationship with the American people. And, we want to get back there. And, I think what you see here is a real bipartisan interest in getting this done.

I know you probably hear, here we go again, right? We are going to testify and we are going to tell our story and nothing happens. You have 75 cosponsors on the privacy bill last year and we did not get it done.

I am here to tell you that I think with the leadership here of Senator Shelby and Senator Brown and the commitment of this Committee, we are going to get this done for you. So, it is critically important that we know what your priorities are, and I applaud—I think Senator Corker took you through a couple that he sees and hears about, we all hear about, and I think Senator Crapo said, OK, here it is, and I hope that you share that document with all of us because we want to get this right.

So, with that—that was kind of my first line of questioning. What two or three things are the highest priority, will take the most amount of burden, give you the biggest bang for the buck, that we know we can do without creating an environment of systemic failure or without unraveling necessary controls to make sure that we do not have a repeat of 2008.

So, I am going to ask you a little different question. We hear all the time about trickle-down of best practices, right. So, all of a sudden, someone comes in and says, well, we just examined Wells and Wells is doing it this way, so we want you to do it this way. So,

that examiner piece, that fear of the heart attack letter, or as you explained, what happens when you do not have someone who can be a monitor or adjust what a maybe overzealous examiner would do, that is also something, and that is a little tougher for us to get at. And, so, I would like to examine that a little bit more, on what you think would be—you obviously did not like the ombudsman suggestion, so I am looking for alternatives to deal with the examination issues that you have, and we can start with you, Mr. Blanton.

Mr. BLANTON. You know, you are right. That is a very, very difficult question to ask because there are so many—with so many examiners at this, so many different approaches on each exam. But, we do come into areas such as, in my bank, are you stress testing your loan portfolio? Well, I am not required to do that, but, they say, well, yeah, but you really need to. And, I understand where they are coming from, but there are just some things—my bank does not represent a risk to anything. I mean, I am sorry. If I go away, there is nothing in this economy that has changed. And, I think, therefore, I need to be regulated and examined in that same way.

Senator HEITKAMP. But, your community will change.

Mr. BLANTON. My community will change, yes, ma'am. It most certainly will. But, I think I need to be regulated that way and I need to be examined that way, to where it meets my risk profile.

Senator HEITKAMP. Some kind of change that we can make here is what I am after, where you would feel comfortable that you had a legitimate second look from an examiner.

Mr. MURRAY. Yes. We believe that an independent process is highly needed for the examination process. We do not really feel like in the credit union world we have an effective appeals process right now. We do not have an ombudsman that we feel we can go to. Our appeals process is up the food chain of the examiner that oversees us. So, it does not work, it is not effective, and, therefore, it is not utilized.

And, you are absolutely right about the best practices trickle-down effect. It is very real and it is very influential, and it happens from all levels. You know, one of the things we are dealing with in the credit union world right now is some perceived notion that interest rates are going to explode in the very near future, and so we are being asked to shock test our balance sheets for incredibly high interest rate shocks, well beyond what is called for in any regulation. That request is coming from examiners who are getting it from higher up in the agency. That is unreasonable, it is illogical, and it costs a lot of time and money. And, we can receive a nice ding on our examination if we either do not do it or if those results do not come out favorably.

Mr. BUHRMASTER. Best practices is real. It happens. We get asked to do reports, not because they are required by regulatory reasons, but they are required by one examiner, and then that report stays with you and that—it is like snowflakes. I mean, you are from North Dakota. You understand this. You walked out this morning and it was beautiful. It was snowing. There was light. But, then you go out to Buffalo, New York——

Chairman SHELBY. Go to North Dakota.

Mr. BUHRMASTER. For me. But, you go out to Buffalo where they have six feet of snow, and that is not, and that is what we have got here, is the cumulative effect.

Now, it is the cumulative effect at these examinations where they are constantly—they are in your house. It is not every 12 months or 18 months. They are there all the time. I get a quarterly call from my examiner. I am submitting paperwork every quarter to them. They are with us. If you move that exam cycle—this is something that you can do—move that exam cycle to 24 months for one and two banks, one and two CAMELS-rated banks, that is going to provide us some relief. That is going to give us greater time to work with the regulators, work through this process. We will not have to jump to the ombudsman so fast because we have got another exam coming up.

Mr. TEMPLETON. I concur with Mr. Buhrmaster's suggestion to increase the exam schedule timeframe. That gives us more time to do things, more time to move the ship.

In terms of the ombudsman, I think the ombudsman could be a good thing just because it is somebody independent watching, OK, and sometimes knowing there is somebody watching makes you do things slightly different. And, it is always a relief valve. In my institution, in 40-plus years, I have only had one or two examiners that I have had difficulty communicating with, and even though, I would not have needed to go to an ombudsman, because it was not that severe.

So, I think one of the first things in the examination process needs to be to try to establish a meaningful dialogue between the examiner and the institution. Sit down and talk about, what are we trying to accomplish here? What are you looking for? What do you want? Let me know when you have headaches. Let me know when you have problems. And, a lot of that can go a long way for easing pains.

Now, there is always a rogue financial institution who does not want to talk to an examiner, sees them as their enemy. You have got a rogue examiner on the other side. So, it is not a perfect world, but communication starts it toward the right place. An ombudsman is just that little safety net hanging there, just in case.

Mr. CALHOUN. I think the real key is where we started here, and it is targeting this relief to community financial institutions. They do have a different model, and that can call for different approaches. But, once these things get blurred and say, you know, we are going to change the system for everybody, even if they are $100 billion, $500 billion, that is a different banking model. It is not the relationship lending. It is not the community focus. And, so, these need to be targeted. I mean, 90 percent of community financial institutions are a billion dollars or less. That is very different from whence people were talking $50 billion or $100 billion, as sometimes gets tossed around.

Chairman SHELBY. Senator Warren.

Senator WARREN. Thank you, Mr. Chairman.

Folks in Massachusetts are really sensitive about snow analogies right now.

[Laughter.]

Senator WARREN. Where it is 77 inches and it is supposed to start snowing again this afternoon, so——

We have heard a lot today about how smaller banks are being smothered by unnecessary regulation, supposedly because of Dodd-Frank rules like the new mortgage rules that went into effect in the first quarter of 2014. Now, I have been looking for some hard data to support that claim. According to the latest report from the FDIC, the banking industry as a whole posted earnings of nearly $40 billion in the third quarter of 2014. That was a 7.3 percent increase relative to the third quarter of 2013. In other words, the banking industry did substantially better after the mortgage rules took effect in January of 2014.

And, here is the kicker. Community banks did even better than the industry as a whole. According to the FDIC, year over year community bank earnings up were nearly 11 percent compared with 7 percent for the industry as a whole.

So, Mr. Blanton, if, as you claim, community banks were particularly hard hit by Dodd-Frank's new rules, why are they making more money since the rules went into effect and doing better than the big banks?

Mr. BLANTON. Well, I do not really think there is necessarily a direct correlation between the mortgage rule passing and the profits of a bank.

Senator WARREN. Well, I thought that was exactly what your testimony was, as I read it, and that is that the rules were tangling up the community banks so that the community banks could not do business, and yet their profitability seems to suggest they are doing better than ever after the regulations went into effect.

Mr. BLANTON. Well, there again, I do not think that it is because of the regulation that the banks are doing better. I mean, it is tangling up our process to do mortgages. It is making it much more difficult. It is costing us quite a lot. Your statistics on the profits of our industry are right. We have done very well. But, if you go back and average over the last 10 years, it has been a very difficult process, and just now, we are beginning to get some efficiencies and come back into the market and be successful and we see these as constraints for us to where we are having a hard time continuing to have that momentum.

Senator WARREN. Well, you know, I appreciate that, but like I said, the numbers show you are really doing pretty well after these regulations. We know that all of the big bank lobbyists love to come into our offices and talk about how community banks are being crushed and they need our help, but a lot of the times, the legal changes that they are asking for are not really about helping community banks, and here is an example.

Mr. Blanton, in your testimony, the ABA's very first request in the name of community bank regulatory relief is a bill that would allow an insured depository institution of any size to satisfy the QM rule as long as they held the loan in portfolio. As you know, under the current rule, banks with under $2 billion in assets that issue fewer than 500 mortgages a year can already satisfy the QM rule for any loan that they hold on portfolio. The CFPB just proposed raising that threshold to 2,000 loans a year. That is going to cover the vast majority of community bank mortgages.

So, just give me a sense here, Mr. Blanton, if Congress passed this bill that the American Bankers Association wants, how many community bank mortgages would become eligible for QM that are not currently eligible, or under the CFPB rules would be eligible, and how does that stack up against the number of mortgages held by Wells Fargo, Citibank, JPMorgan, and the other giants that would become eligible under this change in the rules?

Mr. BLANTON. Well, I think, in the change in the rule that we are currently supporting, I would go back to the argument that if I am holding that loan or they are holding that loan on their books, they are taking all the risks.

Senator WARREN. I am not asking you the question about whether or not you think it is a good rule. I am asking you the question about the impact. I am asking you how many mortgages currently are held or are being issued by community banks that are not—do not have an exemption right now and that would be affected by this rule versus the number of mortgages that are held by Wells Fargo, JPMorgan, and other large financial institutions.

Mr. BLANTON. Well, for a community bank, we would certainly—if they raise that threshold, it will certainly exempt a whole lot of our mortgages that we are holding.

Senator WARREN. You have a whole lot of mortgages outside the CFPB's proposed 2,000 mortgage threshold?

Mr. BLANTON. No, ma'am, but we would add—we would be able to make those loans, then, if they are——

Senator WARREN. And how many for the banking giants?

Mr. BLANTON. Umm——

Senator WARREN. They are part of your organization. Maybe you could just get back to me——

Mr. BLANTON. Yes, ma'am.

Senator WARREN.——on that one. That would be helpful.

You know, the financial performance of the community banks shows that Congress and the regulators, I think, have done a pretty good job of tailoring the rules to protect community banks. We should be very skeptical of regulatory relief bills that are promoted as helping small banks but that are pushed by ABA lobbyists for the big banks.

If we really want to help the community banks, let us start by getting rid of the $85 billion a year too-big-to-fail subsidy that we give to the biggest banks year after year. Small banks are not getting that. Or, let us start by holding big bank executives accountable for committing fraud, like we do with small bank executives for committing fraud. Those are the kinds of changes that would help level the playing field for our community banks.

Thank you, Mr. Chairman.

Chairman SHELBY. Mr. Calhoun, I believe you stated earlier that the CFPB has to review, quote, "every single regulation every 5 years." I do not believe that is correct. What the statute actually says is that the CFPB has to review each significant rule every 5 years, not every rule.

Mr. CALHOUN. I stand corrected.

Chairman SHELBY. OK.

Mr. CALHOUN. I think they broadly interpret the word "significant," though, and it would apply to the vast bulk of their rulemaking.

Chairman SHELBY. Just for the record.

Along these same lines, it is my understanding that the Federal Reserve, and I am reading this, the Federal Reserve System and the Conference of State Bank Supervisors, CSBS, reported earlier in 2014 that many—many—community banks found qualified mortgage and ability to repay rules to be particularly burdensome. In fact, according to the CSBS survey in this study, 15 percent of active mortgage lenders noted 80 percent or more of their one- to four-family mortgage loans would not meet qualified mortgage, QM, requirements.

If a loan is performing and you know the customer—and you know the customers—you would not exist as banks, and you know them—you should be able to make that loan. Otherwise, you are driving that people, as has been pointed out, into areas where they are going to be extorted and everything else. We need to give you some relief. I really believe this.

Mr. CALHOUN. Mr. Chairman, if I could clarify for the record, also——

Chairman SHELBY. Yes.

Mr. CALHOUN.——on the QM proposal that CFPB has currently put out, it actually is to allow an unlimited number of portfolio loans by community banks to qualify for QM status. The 2,000 threshold is they can make 2,000 nonportfolio loans. But, that does not apply to the limitation of how many portfolio loans would qualify for QM status. So, that rule really goes very, very far in providing flexibility to community banks——

Chairman SHELBY. Mr. Buhrmaster, you are in the banking business. You know every day what comes and goes.

Mr. BUHRMASTER. Yes.

Chairman SHELBY. Go ahead and comment.

Mr. BUHRMASTER. Mr. Chairman, if the QM rules were revised to allow portfolio loans to be counted as QM, that is consumer protection from what you said. We have got people that are not meeting those QM standards, the ability to repay, that are being forced to go to other places that do not follow the proper rules——

Chairman SHELBY. And never will.

Mr. BUHRMASTER.——and never will. And, to the point of the 2,000 limit, you know, I have visited two banks that are over that—I am sorry, the $2 billion limit. I visited a bank in Montana, a bank in Nebraska that have rural offices that sometimes are the only offices in those towns, and they write these nonconforming loans. And, it has become more difficult for those banks to hold those on their books if they are not QM. So, we believe that exemption should be higher.

Again, it is consumer protection. You want people coming with the community banks who have their own money on the table when a loan fails.

Chairman SHELBY. Thank you.

Senator Brown.

Senator BROWN. Thank you, Mr. Chairman. A very good hearing. I appreciate, again, your calling it, and all five of the witnesses have contributed a great deal today, all five of you. Thank you.

I mention Mr. Blanton's comments about the son or daughter of a longtime customer friend, community leader, whatever, and that those loans, you just are not likely to make those loans anymore. I think the discussion that a number of you have had about the QM rule providing legal liability protection shifts the burden to the borrower to show that a lender knew they could not pay back the loan.

One of the things you said was the son or daughter does not really qualify for the loan, which is a pretty telling statement for a banker to make, understanding, though, that you can go ahead and make that loan. You just do not have the legal liability protection afforded to you by the QM. So, nobody is saying—putting aside even the expansion of the rule from 500 to 2,000, nobody is stopping you from doing that loan. You just do not do—you know, the hand of big Government is not telling you you cannot do it. It is just saying you do not get the legal protection afforded by QM.

I think it is important to note that, and I think your comments, other comments that several of you have made point to the issue of the Consumer Bureau raising the number from 500 to 2,000. And, I think we all like that. I mean, I like the idea that even—your bank, I understand, Mr. Blanton, is one billion and—what size?

Mr. BLANTON. One-point-eight billion.

Senator BROWN. One-point-eight billion, and you make—you make, typically, how many loans a year?

Mr. BLANTON. Total loans or mortgage loans?

Senator BROWN. Mortgage loans. I am sorry.

Mr. BLANTON. Mortgage loans, about 300.

Senator BROWN. OK. So you are already really under the consumer level. So, understanding—I mean, I know a lot of community bankers in my State, dozens and dozens, and pretty much all of them would fall under the QM portfolio standards of 2,000, and most of them already under the 500.

But if, Mr. Calhoun, you would briefly describe, what are the dangers of overall QM—understanding the ABA, when Mr. Blanton is here speaking for the small banks and sort of echoing the words of Mr. Buhrmaster, that is one thing, but if he is here representing the largest, particularly Wells Fargo and those that are doing huge numbers of mortgage loans, it is a different story. What is the danger of the largest six or eight banks in the country, or even some of the more mid-size but larger on that edge, on that end, banks doing sort of unlimited QM protection if they keep it in portfolio?

Mr. CALHOUN. As we saw in the crisis, a number of the very large banks had business models where they made very risky loans, the loans with no doc, no income, no assets, and also loans with big teaser payments that jumped up dramatically and the only way you would stay in the loan is refinancing if house prices went up. Two examples of those were Washington Mutual and Wachovia, and their portfolio lending was the major factor in taking down both those companies, presenting systemic risk, and also lots of borrowers lost their homes there. And, so, there is a real——

Senator BROWN. So, you like the number 2,000? Is that a good number that we all can agree on?

Mr. CALHOUN. So, again, to be clear, the CFPB rule is even much larger than that. It says you can make 2,000 loans that you sell to the market plus unlimited number, no cap at all on the number that you put on your portfolio.

I would, if I could, just raise one point that is very concerning, is a number of the legislative proposals and even the CFPB rule and their expanded proposal apply to nondepositories equally. Treat them exactly the same, the folks down the street that we are worried about people going to instead of the community banks, get the same relief under some of these proposals, and that is a key change that needs to be made as this goes forward, because it is a very different world for these loans to be made by supervised depository institutions versus made by many of the people who did the reckless lending that started the whole financial crisis.

Senator BROWN. OK. Mr. Buhrmaster, I am going to ask you a question. Another story broke this week of alleged misconduct with one of the world's largest banks. The Governor of the Bank of England in a recent speech said the scale of misconduct at some financial institutions has risen to a level—again, not talking at all about any of you—has risen to a level that has the potential to create systemic risks, unquote. Pretty troubling statement. He went on to say—Mark Carney is his name—it threatens to undermine trust in financial institutions and markets, eliminating some of the hard-won benefits of the initial reforms.

Mr. Buhrmaster, does the continued misconduct by some of the largest banks in this country on Wall Street and some of the largest banks in the world, do they have a negative impact on community banks and your customers?

Mr. BUHRMASTER. It certainly does. When—I mean, I am from New York and I get compared to the Wall Street banks. I mean, people get confused, upstate, downstate. So, naturally, it rubs off on us.

Senator BROWN. Nobody confuses upstate New York——

[Laughter.]

Mr. BUHRMASTER. Thank you.

Senator BROWN. Nobody where I come from. Maybe they do if you live in Rochester, I do not know.

[Laughter.]

Mr. BUHRMASTER. But, the misconduct of some of the largest banks, when you look at that business model, defines that they have to pay where they purposely choose to break the law or violate regulations. It is a budget item for them and it does affect us because it results in these type of regulations we are here trying to get overturned. And, if they continue to have this kind of misconduct, and if they continue not to be held personally responsible—I mean, when a crime is committed, it is not an institution. It is somebody there that is making a decision. But, yet, none of the largest banks have been held accountable.

When the FDIC is suing small banks' directors for certain things but they will not sue the largest six banks for the same type of things, it says there is a different set of rules for different players and it is affecting us. We need the regulatory relief that has come

from that misbehavior. It has fallen on us. That is why it affects us. And, every time there is a headline, it makes it harder to get this regulatory reform through.

Senator BROWN. I could not agree more.

Last question, and thank you for your indulgence, Mr. Chairman. Mr. Murray, you state in your testimony that changing the structure of the Consumer Bureau, the CFPB, by stripping its independence, changing its leadership from a director to a board, would reduce burden for small institutions. I would like to ask each of the five of you—start with Mr. Murray, then Mr. Blanton, and then work across, and then finally Mr. Calhoun—how does changing the structure—I am confused. I do not quite see that. How does changing the structure reduce the burden that, in your case credit unions, in the others, if you agree with that, at the banks.

Mr. MURRAY. Sure. We just believe that it creates an environment for more sensible rulemaking, for collaboration, much like among this Committee, from different minds, whereas when you have one person in charge of the entire Bureau, who sets that agenda? One person, essentially. And, so, we just feel like it is a more common sense approach to coming up with common sense regulation, and so——

Senator BROWN. Do you have any specifics? Any of you, do you have any specifics on why that would be, I mean, what you would get—what you would get different coming out of there?

Mr. MURRAY. CFPB was originally set up, obviously, by Dodd-Frank, and given a very specific set of marching orders in Dodd-Frank. But, then, after that, after that all goes away, what does CFPB do after that and who sets that agenda? Where does that come from? And, that is our concern, and so we feel like a board——

Senator BROWN. Do you suggest changes in the Department of Labor, instead of having one Cabinet Secretary, or the Department of Health and Human Services, or, for that matter, the President of the United States? I mean, should we have—I mean, does that structure make more sense to run our country?

Mr. MURRAY. Well, you know, our Government is set up on a series of checks and balances and that is what——

Senator BROWN. Well, I would say the Consumer Bureau has been hauled in front of the House Financial Institutions Committee about every month or two for oversight, and there are many in this—that we got that—a lot of you working together got some rule changes out of them.

OK. Mr. Blanton, your thoughts, and then Mr. Buhrmaster, Mr. Templeton, and Mr. Calhoun.

Mr. BLANTON. OK. First, I wanted to make one correction. When I said the number of loans I originated, I was thinking of the dollar value. We originated about 1,200 to 1,400 loans a year, so——

Senator BROWN. OK. So, you will still be under the 2,000——

Mr. BLANTON. Still be under it, but I did want to make that clarification.

Senator BROWN. And you are larger than most community banks——

Mr. BLANTON. Yes, I am.

Senator BROWN.——by a lot.

Mr. BLANTON. Yes, I am.

We support a system such as the FDIC Board of Governors. It has worked very well for the FDIC as far as the—we think that that would be a much better system to govern such an important agency as the CFPB, and with that set of different Governors, you get different views and opinions and you get to see a consensus work as opposed to one particular person's direction or whim as to how they want something done. So, we operate well under the FDIC and we think that system works very well as——

Senator BROWN. Do you like the independent funding of FDIC?

Mr. BLANTON. Pardon?

Senator BROWN. Do you like it that FDIC has independent funding, not coming through Congress?

Mr. BLANTON. Umm, no, I do not. I think the way the current system works with the FDIC is correct.

Senator BROWN. Oh, OK. So——

Mr. BLANTON. But, I like the way the Board of Governors works and the way that it oversees that——

Senator BROWN. So, independent funding is OK for the Consumer Bureau. You just want a board with the Consumer Bureau.

Mr. BLANTON. Well, no, I do not agree. I am sorry. I do not agree with the funding of——

Senator BROWN. The funding is OK with FDIC that way, but you want to change the Consumer Bureau to a different funding.

Mr. BLANTON. Yes.

Senator BROWN. OK.

Mr. BLANTON. A more accountable funding.

Senator BROWN. But, why not change the FDIC to more accountable funding, then?

Mr. BLANTON. I guess because the system is working. We are pleased with that system.

Senator BROWN. OK. Mr. Buhrmaster.

Mr. BUHRMASTER. When you are setting a system up, you are not setting it for an individual, an individual personality. You are setting it up for the long term. And, we have had a wonderful relationship with Director Cordray. He has been very receptive to community banks' needs. But, a good example is an interview he just gave in the American Banker recently—in fact, I believe it was this week—where he talked about the difficulty of the process he had in dealing with the exemptions that were just granted on QM. It was his influence that helped bring a different point of view to the table. We may have a different director some day, and having different views at the table when you are dealing with consumer protection items, it keeps the pendulum from swinging too far.

You know, that five-member panel on the FDIC, a lot of what FDIC did in the past was types of consumer protection, whether it is regulating the banks in order to keep the consumers safe or going directly for those regs. Having that—having those different views helps keep things centered and keeps things reasonable.

Senator BROWN. Mr. Templeton.

Mr. TEMPLETON. To echo what Mr. Buhrmaster said, from the conceptual stage, and again, you have to divorce concept and reality. But, conceptually, three or five people coming together to achieve a goal are going to bring different perspectives, different

ideas. There is going to be compromise. There is going to be discussion. There is going to be all sorts of dialogue as you move toward an end result. If you have one person, it just is an agenda. That person may seek input from outside, but it still becomes one person's agenda. So, multiple heads bring greater wisdom.

Another thing that it possibly would bring, and not that you could not do it with a single individual, but it would cause a formal agenda to be released so that, ahead of time, people would know what is going on. Now, that could conceivably be done, but with the board structure, you would need an agenda, and I think the light of day begins shining in. People get time to be prepared and develop concepts and ideas.

Senator BROWN. Fair enough.

Mr. Calhoun, before you respond—and keep it as brief as you can, I apologize—because you made a statement earlier that I just wanted to give you a chance—I have heard you testify a lot, and I have never heard you say something that was kind of not correct, and I want to make sure you get a chance to kind of clarify. You said the CFPB every 5 years is required to review its major regulation. It is—what I think you meant to say, and give you a chance to correct, is 5 years after a new regulation. It is not every 5 years. It is that one time, just to clear the record. Is that your understanding?

Mr. CALHOUN. Yes.

Senator BROWN. OK. OK. That is my—now, answer that other question, and then I will turn it back. Again, thank you for the Chair's indulgence.

Chairman SHELBY. Thank you, Senator Brown.

Senator BROWN. Well, I am sorry, and give him the——

Chairman SHELBY. Yes.

Mr. CALHOUN. So, very quickly, we strongly support the single director. It was the failure, in fact, of the Federal Home Loan Bank Board that led to having a single director being one of the primary reforms for FHFA. And, we believe strongly that the single director will be far more responsive to community financial institution concerns. As we have seen with almost every commission, they become very quickly big bank-centric. If there are five nominees for a commission, the CFPB, there are not going to be four of them that are going to be representing consumer financial institutions, maybe one. We just had to fight to get one on the Fed out of seven spots.

And, there has just been a natural tendency, as we have heard from testimony today, that the commissions focus on the biggest institutions and have less receptivity to community financial institutions. So, that is one of the reasons that we strongly support the current structure. We also note it has the FSOC oversight and the required consultation with other prudential regulators.

Senator BROWN. Thank you, and again, Mr. Chairman, thank you for allowing me to go over my time.

Chairman SHELBY. Thank you. I thank all of you. I think we have had a very good hearing and I appreciate your willingness to be here, to be forthright with us, because that is what we need.

I am going to invite you to supply in writing for this Committee any additional thoughts or information that you may have for our record that will help us to formulate the right thing here.

I also invite the members of your respective organizations to contact us directly here at the Committee with any concerns or ideas that they may have for reform. You are out there in the marketplace. The Members of this Committee, I think, would welcome input from individual financial institutions from all over this country as we consider comprehensive regulatory relief. If you have a concern, we want to hear it.

Thank you again for your appearance here. We are going to try to be responsible here.

The Committee is adjourned.

[Whereupon, at 11:46 a.m., the hearing was adjourned.]

[Prepared statements, responses to written questions, and additional material supplied for the record follow:]

PREPARED STATEMENT OF R. DANIEL BLANTON

CHIEF EXECUTIVE OFFICER, GEORGIA BANK AND TRUST
ON BEHALF OF THE AMERICAN BANKERS ASSOCIATION

FEBRUARY 12, 2015

Chairman Shelby, Ranking Member Brown, my name is Daniel Blanton, Chief Executive Officer of Southeastern Bank Financial Corporation and Georgia Bank & Trust, in Augusta Georgia. I am also the Vice Chairman of the American Bankers Association (ABA). I appreciate the opportunity to be here to present the views of the ABA regarding regulatory relief for small financial institutions. The ABA is the voice of the Nation's $14 trillion banking industry, which is composed of small, midsize, regional and large banks that together employ more than 2 million people, safeguard $11 trillion in deposits and extend more than $8 trillion in loans.

Georgia Bank and Trust is a $1.8 billion community bank established in 1989. We have 12 branches serving the Augusta area and extend $975 million in loans to our local communities.

ABA appreciates the opportunity to be here today to talk about how the growing volume of bank regulation—particularly for community banks—is negatively impacting the ability of banks throughout the Nation to meet our customers' and communities' needs. This is not a new subject, yet the imperative to do something grows every day. Community banks are resilient. We have found ways to meet our customers' needs in spite of the ups and downs of the economy. But that job has become much more difficult by the avalanche of new rules, guidances and seemingly ever-changing expectations of the regulators. This—not the local economic conditions—is often the tipping point that drives small banks to merge with banks typically many times larger. The fact remains that there are 1,200 fewer community banks today than there were 5 years ago—a trend that will continue until some rational changes are made that will provide some relief to America's hometown banks.

Each and every bank in this country helps fuel our economic system. Each has a direct impact on job creation, economic growth and prosperity. The credit cycle that banks facilitate is simple: customer deposits provide funding to make loans. These loans allow customers of all kinds—businesses, individuals, governments and nonprofits—to invest in their hometown and across the globe. The profits generated by this investment flow back into banks as deposits and the cycle repeats—creating jobs, wealth for individuals and capital to expand businesses. As those businesses grow, they, their employees and their customers come to banks for a variety of other key financial services such as cash management, liquidity, wealth management, trust and custodial services. For individuals, bank loans and services can significantly increase their purchasing power and improve their quality of life, helping them attain their goals and realize their dreams.

This credit cycle does not exist in a vacuum. Regulation shapes the way banks do business and can help or hinder the smooth functioning of the credit cycle. Bank regulatory changes—through each and every law and regulation, court case and legal settlement—directly affect the cost of providing banking products and services to customers. Even small changes can have a big impact on bank customers by reducing credit availability, raising costs and driving consolidation in the industry. Everyone who uses banking products or services is touched by changes in bank regulation.

The onslaught of regulatory changes has already had an impact. For example, 58 percent of banks have held off or canceled the launch of new products—designed to meet customer demand—due to expected increases in regulatory costs or regulatory risks. Additionally, 44 percent of banks have been forced to reduce existing consumer products or services due to compliance or regulatory burden.

It is imperative that Congress take steps to ensure and enhance the banking industry's ability to facilitate job creation and economic growth through the credit cycle. The time to address these issues is now before it becomes impossible to reverse the negative impacts. When a bank disappears everyone is affected. We urge Congress to work together—Senate and House—to pass bipartisan legislation that will enhance the ability of community banks to serve our customers.

In particular, Congress can take action to ensure credit flows to communities across the country by (1) improving access to home loans, (2) removing impediments to serving customers, and (3) by eliminating distortions by Government in the marketplace. In the remainder of my testimony, I will highlight some specific actions under each of these that would help begin the process of providing meaningful relief to help community banks and help bank customers.

I. Improve Access to Home Loans

The mortgage market touches the lives of nearly every American household. Banks help individual consumers achieve lifelong goals of homeownership by giving them access to the funding they need. Without home loans most Americans would not be able to purchase a home.

Banks are a major source of mortgage loans—holding more than $2 trillion in one-to-four family home loans on their books and originating others under Government guarantees. In addition, banks support the housing industry with construction and development loans, and homeowners with home equity lines of credit. Housing construction and development, as well as the transactional activities of buying, selling and furnishing homes, generate both direct and indirect benefits for the economy. These critical services of banks results in more income and jobs in communities, along with a larger tax base for local governments. According to the National Association of Home Builders, the construction of 100 single-family homes will result in $21.1 million in income, $2.2 million in taxes and other revenue to local governments, and 324 local jobs.

It is painfully clear that new regulatory requirements have restrained mortgage lending and have made it particularly difficult for first-time home buyers to obtain a home loan. The complex and liability-laden maze of compliance has made home loan origination more difficult, especially for borrowers with little or weak credit history. Over-regulation of the mortgage market has reduced credit available to bank customers, raised the cost of services, and limited bank products. The result has been a housing market still struggling to gain momentum.

Congress can help reduce needless impediments to mortgage lending that have constrained the banking industry's ability to help first-time home buyers and dampened the growth of prosperity across the Nation's communities. For example, Congress should:

> ***Treat Loans Held in Portfolio as Qualified Mortgages:***
>
> The Dodd Frank Act (DFA) is very restrictive in its definition of "ability to repay" and this is having a detrimental impact on the market and consumer access to credit. In fact, the Consumer Financial Protection Bureau (CFPB) has been forced to delay implementation of some aspects of the rule which would eliminate balloon loans. These loans, which are in virtually all cases held in portfolio, are a useful and in-demand product for many customers, particularly those in rural areas seeking smaller dollar loans and those that do not meet secondary market eligibility requirements. It helps bank manage interest rate risk and without tools like this some borrowers would not have access to mortgage loans at all. While the bureau has recently proposed expanded exemptions for smaller lenders serving rural and underserved areas, more relief is needed for lenders and borrowers in all areas of the country.
>
> ABA supports legislation (similar to H.R. 2673 in the 113th Congress) that would deem any loan made by an insured depository and held in that lender's portfolio as compliant with the Qualified Mortgage rule under the DFA (so long as the loan is not sold). The Qualified Mortgage or QM label is given to loans which can be shown to meet the qualifications of the Ability to Repay provisions of DFA. Loans held in portfolio are, by their very nature, loans which can be repaid; otherwise they would present safety and soundness concerns and would not be allowed by a lender's prudential regulators.
>
> Simply put, banks would not stay in business very long if they made and held loans on their books that cannot be repaid; they hold all the risk that a loan might default. This is a common sense approach to showing that a loan has been properly underwritten and meets the QM and ability to repay requirements of the DFA without imposing additional challenges to borrowers and lenders in the lending process.
>
> ***Eliminate the Excessively High Life-of-Loan Liability:***
>
> Not only are the rules complex and liability-laden, the level of liability is both high and often extends for the life of the loan. A liability with such a long life will give any lender pause when considering any but the lowest-risk borrowers. Why should ability to repay liabilities hang over a lender's business for 20 years or more into the life of a 30-year loan? Common sense suggests that any mortgage loan that has remained current for a number of years has certainly demonstrated the borrower's ability to repay. Congress should replace the ATR life of loan liability with a more reasonable

term so that liability ends after a loan has performed for a reasonable number of years.

Establish an Effective Appeals Process to the Definition of a Rural Area:

The definition of rural and underserved is critical and can dramatically affect banks and the communities they serve. The CFPB has already recognized this and has used its DFA discretionary authority to exempt certain loans from the qualified mortgage rule. This has been very important to accommodate community banks that make short-term balloon loans as a means of hedging against interest rate risk. However, the exemption applies only if, during the preceding calendar year, the creditor extended more than 50 percent of its total covered transactions that provide for balloon payments in one or more counties designated by the Bureau as "rural" or "underserved." Thus, the definitions used can be limiting and hurt mortgage customers that are inevitably in counties that may have been inappropriate excluded.

ABA supports legislation (like S. 1916 introduced last Congress by Majority Leader McConnell) that would direct the CFPB to establish an application process to have an area designated as a rural area if it has not already been designated as such by the Bureau. An appropriate exemption process is critical to a bank's ability to meet their community's needs since it would help to assure that whatever definition of rural is ultimately used by the CFPB, there would be an avenue to apply to the Bureau to extend the definition of rural in those inevitable cases where a county may have been inappropriately excluded.

Mandate a Study of the Basel III Capital Requirements Impact on Mortgage Servicing Assets:

Implementation of Basel III is disrupting the market for mortgage servicing rights by imposing punitive capital requirements that are causing many banks to sell these assets, usually to nonbank mortgage servicing firms that have little connection with the original borrowers. ABA supports legislation which requires the banking regulators to study the overall impact of these requirements on the safety and soundness of the banking system, including the impact on the value of such assets as sales are required; the financial stability of nonbank purchasers of mortgage servicing assets; and the risks posed by shifting servicing duties from the banking industry to nonbank entities. The regulators should be required to report to the committees of jurisdiction within 1 year on recommendations for legislative and/or regulatory changes to address concerns identified by the study, and steps to implement the provisions should be halted until Congress has the opportunity to review the study and act.

Encourage the Federal Housing Finance Agency to Reconsider its FHLB Membership Rule:

For more than 80 years Congress has maintained eligibility requirements for lenders to join the Federal Home Loan Banking system. On several occasions, including in recent years, Congress has even taken actions to expand eligibility for members in certain ways. Currently, the FHFA has proposed restrictions which might limit the ability of banks of all sizes, including community banks, from retaining this critical source of liquidity. The ABA does not object to a consideration of the best way to regulate new business structures among Home Loan Bank system members that might otherwise impose risks on the system. However, the system should retain what is essentially a self-enforcing discipline that Congress created when it first established the system. The simple matter is members cannot borrow from the Federal Home Loan Bank system unless they have eligible collateral that is contemplated by the statue. ABA will continue to work with Members of Congress to ensure that the Federal Housing Finance Agency follows congressional intent and does not unnecessarily restrict access to vital liquidity provided by the Federal Home Loan Banks.

II. Remove Impediments to Serving Customers

Rules and requirements surround every bank activity. When it works well, bank regulation helps ensure the safety and soundness of the overall banking system. When it does not, it constricts the natural cycle of facilitating credit, job growth and economic expansion. Finding the right balance is key to encouraging growth and

prosperity as unnecessary regulatory requirements lead to inefficiencies and higher expenses which reduce resources devoted to lending and investment.

The key to changing this consolidation trend is to stop treating all banks as if they were the largest and most complex institutions. Financial regulation and examination should not be one-size-fits-all. All too often, regulation intended for the largest institutions become the standard that is applied to every bank-Basel III being the most egregious. Such an approach only layers on unnecessary requirements that add little to improve safety and soundness, but add much to the cost of providing services—a cost which customers ultimately bear. Instead, ABA has urged for years that a better approach to regulation is to tailor bank supervision to take into account the charter, business model, and scope of each bank's operations. This would ensure that regulations and the exam process add value for banks of all sizes and types.

By eliminating unnecessary impediments to the natural credit cycle, Congress can help stem the tide of community bank consolidation driven by these unnecessary impediments which negatively impacts every community across the United States. For example, Congress can:

Reduce unnecessary and redundant paperwork:

Congress should require a review and reconciliation of existing regulations that may be in conflict with or duplicative of new rules being promulgated by the banking agencies, or which in their application badly fit the variety of institutions that make up the banking industry. This would help to eliminate conflicts among different regulations, thereby eliminating additional and unnecessary compliance burdens. It would also result in more effective policies. Congress should also (among other things):

- Eliminate unnecessary currency transaction report filings;
- Provide greater accountability for law enforcement's use of the Bank Secrecy Act data; and
- Eliminate redundant annual privacy policy notices by passing S. 423

Create a more balanced, transparent approach to bank examination and regulation:

Congress should expand the number of banks eligible for an 18-month exam cycle for highly rated community banks. This would reduce significantly the resources required to deal with yearly examinations by the regulators. The Comptroller of the Currency, Thomas Curry, publicly stated such a change would reduce burden on well-managed community institutions and would also allow the agencies to focus their efforts on institutions that may present supervisory concerns.

Congress should also:

- Provide an independent appeals process for bank examination decisions resulting in better accountability;
- Require the Securities and Exchange Commission and the Bank Regulators to perform cost-benefit analyses before issuing new rules; and
- Revise the cost-benefit test for rules proposed by the Commodity Futures Trading Commission.

Limit burdensome trickle-down of complex bank regulations:

Congress should support legislation that prevents the "trickle-down" of complex bank regulation onto smaller and mid-sized banks. For example, Congress should:

- Require targeted rulemaking by regulators that focus on the purpose of the rule, appropriately adjusted to the risk footprints of banks;
- Remove arbitrary regulatory thresholds not corresponding to a bank's risk and business model;
- Exempt small banks from Commodity Futures Trading Commission clearing requirements which would improve their ability to manage risk within the firm;
- Eliminate unnecessary public stress test disclosures for mid-sized banks; and
- Ensure capital rules designed for systemically important financial institutions are applied only to banks that are truly SIFIs, based on multifactor assessments of systemic risk, not merely asset size.

III. Eliminate Distortions by Government in the Marketplace

The banking industry's ability to serve customers is affected by many forces, including regulatory or tax-advantaged nonbank competition and unreasonable legal risks. These forces restrain the credit cycle, add risk and distortions, and impede the banking industry's ability to encourage growth and prosperity within communities.

Nonbank financial institutions offer identical products and services but do so without the same regulatory oversight, consumer compliance or tax treatment. As bank regulations become increasingly restrictive, products migrate from the safety and soundness of the banking system to the under-regulated or unregulated market. This magnifies risk for all who use financial services.

Furthermore, some nonbanks benefit from special tax privileges which have created economic distortions that shift resources and banking activity from taxpaying banks to the tax-privileged sectors. Credit unions and the Farm Credit System are prime examples. Such marketplace tax distortions are neither good public policy nor fiscally responsible.

In addition, unreasonable legal risks faced by banks have restrained the credit cycle. For example, uncertainties surrounding the interpretation of fair lending rules have raised the risks of costly litigation and forced financial institutions to limit mortgage lending operations. Similarly, unjustified and abusive patent litigation and licensing fee demands have drained funds available for lending. These legal risks create no benefit for local communities. Congress should eliminate unreasonable legal risks so that the banking industry can return to the business of banking.

Another potential and serious distortion involves innovations within the payment system by nonbanks. Banks have always protected the integrity of the payments system. As new innovations come forward it is critical that they are within a secure regulatory system that promotes consumer protection and system integrity. Equal access and equivalent regulation are key principles to ensure this.

Congress should:

Support legislation that eliminates Government distortions in the private market by:

- Eliminating the Credit Union industry's special tax treatment
- Ending the Farm Credit System's unjustified tax privileges
- Ensuring agencies do not impose price controls, directly or indirectly

Support legislation to eliminate unreasonable legal risks and impediments by:

- Enacting patent troll reform to reduce the threat of patent abuse
- Removing uncertainties in fair lending rules, such as penalties where there is no intent to engage in unlawful discrimination

Support Taxpaying Bank Charters by:

- Conforming savings and loan holding company thresholds and registration rules with those of banks
- Supporting charter flexibility for mutual banks and Federal savings associations
- Encouraging regulators to charter new banks

Protect the Payments System by:

- Ensuring that all participants—banks and nonbanks—are subject to consistent rules and oversight for consumer protection, safety and soundness and systemic risk
- Avoiding technology mandates
- Expanding information-sharing between public and private entities to fight threats
- Ensuring all parties have consistent accountability to customers before and after breaches
- Holding breached parties responsible for costs of breaches

Conclusion

Community banks have been the backbone of hometowns across America. Our presence in small towns and large cities everywhere means we have a personal stake in the economic growth, health, and vitality of nearly every community. A bank's presence is a symbol of hope, a vote of confidence in a town's future. When

a bank sets down roots, communities thrive. We urge Congress to act now to help turn the tide of community bank consolidation and protect communities from losing a key partner supporting economic growth.

CUNA
Credit Union National Association

601 Pennsylvania Ave., NW
South Building, Suite 600
Washington D.C. 200004-2601

Phone: 202-638-5777
Fax: 202-638-7734

TESTIMONY
OF
WALLY MURRAY
PRESIDENT AND CHIEF EXECUTIVE OFFICER
GREATER NEVADA CREDIT UNION

ON BEHALF OF
THE CREDIT UNION NATIONAL ASSOCIATION

AT THE HEARING OF
THE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
UNITED STATES SENATE

ON
REGULATORY RELIEF FOR COMMUNITY BANKS AND CREDIT UNIONS

FEBRUARY 12, 2015

Testimony
of
Wally Murray
President and Chief Executive Officer
Greater Nevada Credit Union
On Behalf of
The Credit Union National Association
Before the Hearing of
The Committee on Banking, Housing and Urban Affairs
United States Senate
On
Regulatory Relief for Community Banks and Credit Unions
February 12, 2015

Chairman Shelby, Ranking Member Brown, Members of the Committee:

Thank you for the opportunity to testify today regarding proposals for regulatory relief for small depository institutions. My name is Wally Murray, and I am president and chief executive officer of Greater Nevada Credit Union, a federally insured state chartered credit union located in Carson City, Nevada, serving more than 47,000 members. I am testifying today on behalf of the Credit Union National Association, the national trade association for America's state and federally chartered credit unions. CUNA represents approximately 90% of America's 6,500 credit unions and their 102 million memberships.

Credit unions' statutory mission is to promote thrift and provide access to credit for provident purposes to credit union members. This is the mission that credit unions have fulfilled since their inception in the United States more than 100 years ago. The system's size and growth in terms of membership, loans and deposits, and its consistent soundness are indicators that credit unions succeed in fulfilling this mission.

At the beginning of the credit union system's second century, we have a vision that credit unions are Americans' best financial partner. More than 102 million memberships are represented in member-owned cooperative financial

institutions, America's credit unions. The credit union system is very sound, with a system wide capital ratio of 10.8%, and we have a history of being there for credit union members in good times and bad. When the financial crisis threatened the economy and the financial livelihood of many Americans, credit unions were a safe harbor for consumers and small businesses that could not access credit elsewhere; they continued to lend when others were forced to pull back.

As the economy recovers, America's credit union members continue to rely on their credit unions for safe and affordable financial services delivered by institutions that they own; and credit unions continue to deliver tremendous benefits to their members in terms of lower-interest rate loans, and lower-fee or no-fee products and services. Because credit unions are actively fulfilling their mission, consumers – credit union members and nonmembers – benefit to the tune of $10 billion annually.

Credit union employees and volunteers work every day to deliver service excellence to their members, but there are several statutory and regulatory barriers that keep credit unions from more fully serving the savings and credit needs of their members. We want to work with the Committee to remove these barriers. If these barriers are removed, the impact that credit unions could have on the financial lives of their members would be that much more significant and the economic contribution credit unions and their members make would be that much greater.

The Consequences of Doing Nothing

American consumers cannot afford for Congress to do nothing to address this crisis of creeping complexity with respect to regulatory burden. Since the beginning of the financial crisis, credit unions have been subjected to more than 190 regulatory changes from nearly three dozen Federal agencies totaling nearly

6,000 *Federal Register* pages.[1] These numbers do not take into account regulatory changes that may emanate from state regulators. Every time a rule is changed credit unions and their members incur costs. They must take time to understand the new requirement, modify their computer systems, update their internal processes and controls, train their staff, design and print new forms and produce material to help their members understand each new requirement. Even simple changes in regulation cost credit unions thousands of dollars and many hours: time and resources that could be more appropriately spent on serving the needs of credit union members.

Regulatory change presents a particularly difficult challenge for small depository institutions because the fixed cost of compliance are proportionately higher for smaller-sized credit unions and banks than for behemoth banks. Congress and regulators ask a lot of small, not-for-profit, financial institutions when they tell them to comply with the same rules as J.P. Morgan, Bank of America and Citibank. Almost half of the credit unions in the United States operate with five or fewer full-time equivalent employees; the largest banks likely have compliance departments that exceed that number by multiples of a hundred or more. To put the question of size in further perspective, consider that each of the four largest banks in the United States has total assets greater than the combined assets of the entire credit union system. The rules that the Consumer Financial Protection Bureau (CFPB) has promulgated so far have not taken this disparity -- and disproportionate burden -- into consideration as much as we feel it can or should under the law.

This is one of the primary reasons that Main Street financial institutions are disappearing at an alarming rate. The number of credit unions has been halved in the last 20 years – from more than 12,500 in 1995 to just more than 6,500 today.

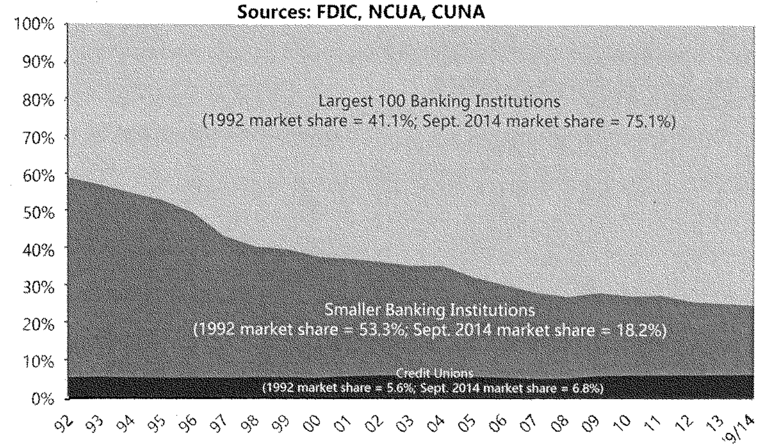
[1] A list of these changes, the agencies which promulgated them and the number of pages of each rule is attached to this testimony.

A similar phenomenon is happening in the banking industry. To be fair, the financial crisis played a part in the consolidation of small financial institutions – in Nevada, for example, there were 25 credit unions at the beginning of the crisis and today there are 18 – but consolidation was also significant both before and after the crisis. Today's consolidation of small financial institutions, much like the pre-crisis trend, is being led by an ever-increasing, never-decreasing, regulatory burden that frankly forces some credit unions simply to give up and find other larger credit unions with which to merge.

When smaller institutions like mine disappear, large banks gobble up market share.

Big Banks Increasingly Dominate Market Share of Total Assets

Sources: FDIC, NCUA, CUNA



The problem is that regulators are, in many cases, applying a one-size-fits-all approach to regulation on depository institutions; and, when there are exceptions or exemptions provided in rulemaking, they are too narrow to be effective. The CFPB's international remittance transfer (IRT) rule is a great

example of the negative consequences of regulation that is too broad and has unintended consequences when applied broadly to credit unions, which did not engage in the activity that brought on the new rules.

CUNA recently conducted a survey of credit unions that offer or have offered IRTs since 2013. Responses to the CUNA survey clearly show the shockingly large impact regulations can have on service provision and consumer costs. The survey reveals that almost half of credit unions (49%) have either stopped offering IRTs (23%) or now turn members away (26%), purposefully limiting the number of IRTs to stay below the CFPB's rule threshold. Another 12% say they are considering discontinuing the service.

Among those who still offer IRT services, one third do so through third-party providers. Fully 71% of these credit unions indicate the cost of providing these services has increased, with 25% saying those costs have increased by 50% or more. Among those that continue to offer IRT services in-house, 56% say they've had to increase prices, with 32% indicating they've had to increase prices 50% or more.

When asked to describe their approach to pricing IRTs, none indicate that they choose prices to earn a significant profit. Overall, 40% say they price to break-even and 44% say they price to make a small profit, while 15% indicate that they lose money on IRT service provision.

The numbers paint a clear picture: as a result of the rule, fewer credit unions are offering remittances; those that continue to offer remittances conduct fewer transactions; and the transactions that credit unions complete are priced higher than they were prior to the rule. It is hard to see how credit union members benefit when their credit unions are forced to discontinue, limit or significantly increase the cost of this critical lifeline service. Given that this was one of the first rules issued by the CFPB and reinforced by the significant concerns that persist with the CFPB's mortgage lending rules, credit union managers and volunteers are

understandably very concerned that the CFPB's potential action on overdraft protection and payday lending products could further jeopardize their ability to effectively, efficiently and affordably provide critical lifeline financial services to those who need them the most.

If Congress does nothing to protect small depository institutions from, and relieve them of, the unnecessary and poorly focused regulatory burden, the trend of consolidation will continue; consumers will have fewer options in the financial marketplace; and the cost of accessing mainstream financial services will increase. This outcome is unacceptable, and Congress can do something about it.

The Barriers Credit Unions Face

Credit unions face many statutory and regulatory barriers as they work to fulfill their mission and fully serve their members. This testimony discusses more than two dozen proposals or issues that Congress should address:

- Congress Should Make Several Improvements to the *Federal Credit Union Act*
  - Improve Credit Union Capital Requirements
  - Restore Credit Unions' Business Lending Authority
    - Increase the Member Business Lending Cap
    - Treat 1-4 Family Non-Owner Occupied Residential Loans as Residential Loans, and Not Credit Union Business Loans
    - Improve Credit Unions' Ability to Engage in Small Business Administration and Other Guaranteed Lending Programs
  - Modernize Credit Unions' Loan Maturity Restrictions
  - Modernize Credit Union Investment Authority
  - Modernize Regulation of Federal Credit Union By-Laws
  - Address Credit Unions' Incidental Powers
  - Clarify Credit Unions' Ability to Offer Prepaid Cards
  - Improve Analysis of NCUA Rulemakings and Require Public Hearings on the NCUA Budget
- Improve the Structure of the CFPB to Achieve Better Results for Consumers and Covered Entities
  - Expand and Specify the CFPB's Exemption Authority
  - Install a Five-Person Board to Run the CFPB

    - Fund the CFPB Through the Appropriations Process
    - Substantially Increase the CFPB Examination Threshold
    - Require Cost-Benefit Analysis of all CFPB Proposals
    - Codify the Credit Union Advisory Council
    - Require Small Business Regulatory Enforcement Fairness Act Panels for CFPB Rulemakings
    - Improve the Definition of Rural and Underserved Areas
    - Enact the Mortgage Choice Act
    - Raise the Points and Fees Limit on Qualified Mortgages Greater than $100,000
    - Standardize the Definition of Mortgage Originator
    - Deem Mortgages Held in Portfolio as Qualified Mortgages
- Enact Examination Fairness Legislation
- Address Issues Related to Federal Home Loan Bank Membership Eligibility
    - Ensure FHLB Membership Eligibility Rules are the Same for Small Credit Unions and Banks
    - Make Privately Insured Credit Unions Eligible to Join the Federal Home Loan Bank System
- Enact the Privacy Notification Modernization Act
- Stop Merchant Data Breaches

This testimony also discusses issues we believe could develop into new barriers for credit unions if Congress does not undertake oversight of them. These include possible proposals from the National Credit Union Administration (NCUA) related to third-party vendor authority and interest rate risk.

Congress Should Make Several Improvements to the *Federal Credit Union Act*

It has been nearly 20 years since Congress enacted meaningful and comprehensive amendments to the *Federal Credit Union Act*. Since the enactment of the *Credit Union Membership Access Act of 1998*, Congress has amended the *Federal Credit Union Act* precisely nine times. These amendments

included restrictions of former NCUA employees,[2] requirements on the use of the NCUA logo,[3] an increase of loan maturity limits on certain loans,[4] authorization for credit unions to provide certain lifeline services to nonmembers within their field of membership,[5] *Bankruptcy Reform Act* conforming amendments,[6] *Housing and Economic Recovery Act* conforming amendments,[7] establishment of the corporate credit union stabilization fund,[8] *Dodd-Frank Act* conforming amendments,[9] additional clarification related to the stabilization fund,[10] and most recently an amendment providing parity with FDIC insurance coverage of trust accounts.[11]

During the same period of time, Congress repealed the *Glass-Steagall Act*, removing the barrier between commercial and investment banking and enacted several bills aimed at removing barriers for small banks to compete against large banks;[12] reduced the frequency of examinations for banks between $200 million and $500 million;[13] provided banks with access to the $700 billion taxpayer funded Troubled Asset Relief Program (TARP);[14] adjusted the deposit insurance base to

---

[2] Public Law 108-458 (December 17, 2004) added Section 206(w). Added a section restricting employment of certain NCUA employees after leaving the agency.

[3] Public Law 109-173 (February 15, 2006) amended Section 205(a), 207(k). Amended sections requiring insurance logo and increased insurance coverage for certain retirement accounts.

[4] Public Law 109-351, Financial Services Regulatory Relief Act (October 13, 2006). Increased certain loan maturities from 12 to 15 years; allowed certain check cashing and money transfer services to be offered and other small housekeeping amendments.

[5] Ibid.

[6] Public Law 109-8 (April 20, 2005) amended Section 207(c)(8)(D). Amended definition to give the NCUA Board more authority to define a "qualified financial contract", which generally is a securities contract. This was part of the Bankruptcy Abuse Prevention and Consumer Protection Act.

[7] Public Law 110-289, the Housing and Economic Recovery Act (July 30 2008) div. A, title VI, § 1604(b)(2), amended Section 207. Minor amendment to changing the term "bridge bank" to "bridge depository institution.

[8] Public Law 111-22, Preventing Mortgage Foreclosures and Enhancing Mortgage Credit Act (May 20, 2009) div. A, title II, § 204(c), (e), & (f) amended Sections 202(c)(2), 203(d) and added Section 217. Created the Temporary Corporate Credit Union Stabilization Fund; temporarily increased share deposit insurance.

[9] Public Law 111-203, the Dodd Frank Act (July 21, 2010) title III, §§ 335(b), 343(b)(1), (3), 351, 362(3) amended Sections 206(g)(7) and 207, title III, § 362(1) and title X, § 1073(d), amended Sections 107, 205 and 206; title IX, § 988(a) amended Section 216.

[10] Public Law 111-382, National Credit Union Authority Clarification (January 4, 2011) §§ 1 & 2, amended Section 202 and added Section 217; § 3 amended Section 216. Authorized NCUA to make stabilization fund expenditures without borrowing from the Treasury; required a study of the supervision of corporates and the use of prompt corrective action.

[11] Public Law 113-252, Credit Union Share Insurance Fund Parity Act (December 18, 2014). Allows NCUA to provide NCUSIF insurance to IOLTAs and other similar escrow accounts.

[12] Public Law 106-102, Gramm-Leach-Bliley Act.

[13] Public Law 109-473, a bill to make a conforming amendment to the Federal Deposit Insurance Act with respect to examinations of certain insured depository institutions.

[14] Public Law 110-343, the Emergency Economic Stabilization Act.

save community banks $4.5 billion over three years;[15] temporarily guaranteed all deposits in banks through the Transaction Account Guarantee (TAG) program;[16] created a $30 billion business lending program for banks under $10 billion in total assets;[17] raised the bank shareholder threshold for registering with the Securities and Exchange Commission;[18] increased the threshold for bank holding companies and savings and loan holding companies to satisfy certain tests to incur additional debt for the purposes of acquiring other banks from $500 million to $1 billion;[19] and ensured that there is a community bank representative on the Federal Reserve Board of Governors.[20]

When the extensive procedural and substantive relief that Congress has provided to banks is juxtaposed with the limited and modest amendments which have been enacted to the *Federal Credit Union Act*, it becomes easy to understand the frustration from many in the credit union system. Congress must ensure the credit union charter allows institutions to fully serve their members' needs in the sophisticated financial services marketplace we have today. The following proposals would help credit unions more fully serve their members while at the same time enhancing the safety and soundness of the credit union system.

Improve Credit Union Capital Requirements

One lesson of the financial crisis is "capital is king" and the measures used to assess the capital condition of financial institutions were imperfect, to put it mildly. Financial regulators, including NCUA, have worked in recent years to impose "better" schemes to assess the health of financial institutions; NCUA's new risk-based capital proposal is its latest attempt in this area. While we appreciate the significant improvements that NCUA has made to the second version of this

[15] Public Law 111-203, the Dodd-Frank Wall Street Reform and Consumer Protection Act.
[16] Ibid.
[17] Public Law 111-240, the Small Business Jobs Act.
[18] Public Law 112-106, the Jumpstart our Business Startups.
[19] Public Law 113-250, a bill to enhance the ability of community financial institutions to foster economic growth and serve their communities, boost small businesses, and increase individual savings.
[20] Public Law 114-1, the Terrorism Risk Insurance Act.

proposed rule, questions persist with respect to whether all aspects of the proposal are consistent with the agency's legal authority, and whether the costs of implementing the proposal outweigh the benefit to the National Credit Union Share Insurance Fund. Stakeholders will continue to weigh in on the rulemaking process, but Congress should seriously consider whether significant changes to the statutory framework need to be made.

The questions for Congress are whether, in a modern financial services environment in which regulators are using scalpels to assess the risk of various asset types:

- Does it make sense for the credit union system to have its leverage ratio hardwired into the statute or would it make more sense for the safety and soundness regulator to have more discretion to develop capital requirements that more appropriately reflect the risk a credit union might present to the share insurance fund?
- Would the safety and soundness of the credit union system benefit if credit unions had access to additional sources of capital in a form consistent with the cooperative ownership structure under which they operate?

We encourage Congress to consider comprehensive reforms to the credit union capital structure, including authorizing NCUA to define what the different net worth levels must be in order to be "well-capitalized," "adequately capitalized," "undercapitalized," and "significantly undercapitalized," based on credit unions' financial performance, current economic trends and other relevant factors.

We also believe that NCUA should have the authority to allow all credit unions to accept supplemental forms of capital. Under current law, approximately 2,000 credit unions, those designated as low-income credit unions, have this authority. Permitting all credit unions to acquire supplemental capital in a manner

consistent with their cooperative ownership structure would enhance the safety and soundness of the credit union system. As we have testified in the past, we believe the legislation that Representatives King (R-NY) and Sherman (D-CA) have introduced to permit credit unions to accept supplemental forms of capital would be a good place to start regarding credit union capital reform.

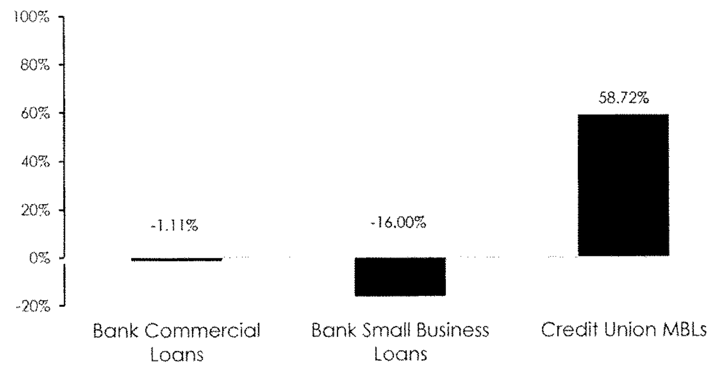
Restore Credit Unions' Business Lending Authority

We reiterate our call on Congress to restore credit unions' authority to lend to their small business members. No economic or safety and soundness rationale has ever been established for why credit unions should be subjected to a cap on small business lending, and we believe Congress should fully restore credit unions' ability to lend to their small business members, as they did without statutory restriction until 1998.

As we have testified many times before, while the small banks were asking for taxpayer money to lend to small businesses, credit unions were pleading with Congress to permit well-capitalized credit unions with a strong history of business lending to lend beyond the arbitrary cap on business lending that is in statute.

The facts are not in dispute. During the financial crisis, banks withdrew access to credit for small businesses while credit unions kept lending.

Business Loan Growth
December 2007 to June 2012
Sources: FDIC, NCUA, CUNA.



Anecdotally, we are aware of several instances in which banks referred business lending customers to credit unions, because they were unable to make the loans themselves.

NCUA has testified in support of expanding the business lending cap several times, most recently this week.[21] The administration has supported expanding the business lending cap.[22] There are more than 500 credit unions for which the cap is a significant operational restriction. These credit unions deserve the opportunity to continue to serve their business members and their communities, and Congress should address this issue.

Increase the Member Business Lending Cap

If Congress is unable to eliminate the cap entirely, we strongly urge enactment of legislation that has been introduced in the last several Congresses

---

[21] Testimony of Larry Fazio, Director, Office of Examination and Insurance, National Credit Union Administration, before the Senate Banking Committee Hearing on "Regulatory Relief for Community Banks and Credit Unions." February 10, 2015.
[22] Letter from U.S. Secretary of Treasury Timothy Geithner to House Financial Services Committee Chairman Barney Frank. May 25, 2010.

to permit Federally insured credit unions to make member business loans (MBLs) in an aggregate of 27.5% of its total assets as long as the credit union: (a) is well-capitalized; (b) can demonstrate at least 5 years' experience managing a sound MBL program; (c) has had MBLs outstanding equal to at least 80% of 12.25% of its assets; and (d) complies with applicable regulations. We believe this is a reasonable approach that ensures that business lending in excess of the current statutory cap is conducted by healthy credit unions with a demonstrated history of sound business lending practices. While it does not get credit unions back to the place they were prior to 1998 when they were not subject to a statutory cap on business lending, it will provide several hundred credit unions with relief to continue to serve their small business members and their communities.

Importantly, raising the cap in the manner outlined above would increase small business lending by as much as $16 billion, helping to create nearly 150,000 new jobs, in the first year after enactment. This level of growth would have been very helpful in the throes of the financial crisis, but even in the recovering economy, this type of growth is important. And, contrary to the banker argument, this lending would not produce a dollar for dollar reduction in bank lending. In fact, the Small Business Administration (SBA) commissioned a study that suggested 80% of additional credit union lending would be new small business lending.[23] This would be a benefit for small business owners and it would not jeopardize the banking industry's share of the small business lending market, which for the last two decades has been approximately 93% of the market.

Treat 1-4 Family Non-Owner Occupied Residential Loans as Residential Loans, Not Credit Union Business Loans

In addition to legislation to modernize credit union business lending, we encourage Congress to address a disparity in the treatment of certain residential loans made by banks and credit unions. When a bank makes a loan for the

[23] Wilcox, James A. "The Increasing Importance of Credit Unions in Small Business Lending." Small Business Administration Office of Advocacy. September 2011. 20.

purchase of a 1-4 unit non-owner occupied residential dwelling, the loan is classified as a residential real estate loan; however, if a credit union were to make the same loan, it would be classified as a business loan and therefore subject to the cap on member business lending under the *Federal Credit Union Act*.

We support legislation to amend the *Federal Credit Union Act* to provide an exclusion from the cap for these loans. Doing so would not only correct this disparity, but it would enable credit unions to provide additional credit to borrowers seeking to purchase residential units, including low-income rental units. Credit unions would be better able to meet the needs of their members if this bill was enacted, and it would contribute to the availability of affordable rental housing.

It is also worth noting that in its recent risk-based capital proposal, NCUA treated these loans differently than commercial loans. Excluding these loans from the business lending cap would provide consistency with the agency.

Improve Credit Unions' Ability to Engage in Small Business Administration and Other Guaranteed Lending Programs

We encourage Congress to improve credit unions' ability to offer SBA and other government guaranteed loans. Specifically, Congress should exempt government guaranteed loans in their entirety from the member business lending cap; currently, only the guaranteed portion of the loan is exempt. Further, Congress should clarify that credit unions participating in Federal and state loan guarantee programs may include terms for such loans as permitted by the loan guarantee programs in both statute and regulations; this would allow credit unions to more fully participate in the SBA's 504 Loan Program.

Modernize Credit Unions' Loan Maturity Restrictions

We encourage Congress to consider legislation that eliminates references in the *Federal Credit Union Act* to loan maturities, leaving it to Federal credit unions to make their own business decisions about maturities of their various loans. As enacted in 1934, the *Federal Credit Union Act* specified a maximum loan maturity

and this provision has continually been amended as new products emerge. There is no overall safety and soundness reason for these provisions to remain in the Act; NCUA should be able to address any particular concerns through general regulatory authority, but more likely through specific supervisory actions. National banks and state chartered credit unions in every state except Alaska, Louisiana and Oklahoma, are not subject to loan maturity limits.

Modernize Credit Union Investment Authority

The *Federal Credit Union Act* currently limits Federal credit unions' investment authority to loans, government securities, deposits in other financial institutions and certain other limited investments. The limitation curtails the ability of a credit union to respond to the needs of its members. We encourage Congress to permit Federal credit unions to purchase investments for their own accounts in bonds, notes, debentures or other instruments and other "investment securities" similar to those authorized for national banks.[24] Similar proposals have passed the House of Representatives in 2006 and 2008.[25]

Modernize Regulation of Federal Credit Union Bylaws

We encourage Congress to modernize outdated credit union governance restrictions to better address the evolving needs of Federal credit unions.

Although we believe that NCUA has this authority, we ask Congress to allow Federal credit unions to devise their own bylaws, which include permitting the boards of directors of Federal credit unions to impose term limits on members of the board and permitting credit unions to adopt policies related to the expulsion of members.

The bylaw provision in the *Federal Credit Union Act* was adopted many decades ago to address the needs of new credit unions. Based on that language,

[24] Under 12 USC section 24 as implemented by 12 CFR 1.
[25] Section 303 of H.R. 3505, 109th Congress, which passed the House of Representatives on March 8, 2006; Section 101 of H.R. 6312, 110th Congress, which passed the House of Representatives on June 24, 2008.

today NCUA issues standard bylaws which must be implemented by all Federal credit unions, regardless of size and complexity, unless individual credit unions seek NCUA approval to amend specific provisions. This is an unnecessarily archaic approach, and the Act needs to be altered to allow NCUA to address bylaws, in general, and to prepare model bylaw language that a Federal credit union can choose to use.

Federal credit union boards of directors should have the flexibility to establish term limits for members of the board in order to allow for a turnover of expertise and a broader representation as membership changes. Providing credit unions with this right does not raise supervisory concerns and should not, therefore, be regulated or restricted by government. We ask Congress to permit Federal credit union boards of directors to decide for themselves whether terms limits are appropriate.

The *Federal Credit Union Act* currently permits a member to be expelled by a two-thirds vote of the membership present at a special meeting, which can be costly to call. While the instances of credit union member expulsion are rare, there have been situations in the past where a more expedited expulsion process would have been warranted, including situations where a member was harassing personnel and creating concerns for the physical safety of staff and other credit union members. Under the current language, a Federal credit union has little latitude to address such situations efficiently and in a timely manner. We ask Congress to provide Federal credit union boards of directors additional flexibility to address these situations by allowing Federal credit unions to adopt and enforce an expulsion policy for just cause and nonparticipation by majority vote of their board of directors. Similar proposals passed the House of Representatives in 2006 and 2008.[26]

[26] Section 310 of H.R. 3505, 109th Congress, which passed the House of Representatives on March 8, 2006; Section 110 of H.R. 6312, 110th Congress, which passed the House of Representatives on June 24, 2008.

Address Credit Unions' Incidental Powers

We encourage Congress to enact legislation to establish the same incidental powers authority for Federal credit unions in the *Federal Credit Union Act* as exists for national banks in the *National Bank Act*.[27] As part of this proposal, NCUA should be directed to implement standards for incidental powers that are no more limited than those relied upon by the Comptroller of the Currency in approving new incidental powers activities for national banks and to consider additional incidental powers for credit unions whenever such powers are approved by the Comptroller.

Clarify Credit Unions' Ability to Offer Prepaid Cards

To ensure that credit unions are able to meet the evolving needs of their fields of membership, Congress should clarify that Federal credit unions can sell prepaid payment cards to persons within their field of membership, similar to existing authority to provide check cashing and remittances services to persons within their field of membership.

In addition, Congress may need to clarify the insurance coverage of prepaid cards issued by the credit union on behalf of a member to nonmembers within the field of membership. We believe legislation Congress enacted in 2014 related to the treatment of escrow accounts could provide NCUA authority to extend insurance coverage to the funds in the master accounts owned by nonmembers; however, we have asked NCUA for clarification of this matter. If NCUA determines that it does not have the authority to extend insurance coverage to these types of accounts, Congress may need to amend the *Federal Credit Union Act* to provide such coverage. Doing so would be consistent with the coverage provided by the Federal Deposit Insurance Corporation.

---

[27] 12 U.S.C. § 24.

Improve Analysis of NCUA Rulemakings and Require Public Hearings on the NCUA Budget

We encourage Congress to require NCUA to complete an extensive cost-benefit analysis before the agency proposes any rule and to provide this analysis with any proposal that is issued for comment. Credit unions fund NCUA and the National Credit Union Share Insurance Fund. It is reasonable that credit unions should be provided with an analysis of the cost and the benefit of proposals the regulator is proposing.

For the same reason, we encourage Congress to require the NCUA Board to conduct an annual public hearing on the agency's draft budget. While we appreciate the opportunity to discuss budgetary concerns with the Board in advance of action on the budget, it is fair and reasonable for the Board to take public comments for the record prior to taking action on a budget that relies on credit union member resources. Conducting such a hearing would represent a very modest burden on the agency and the Board – a handful of hours simply to listen to those whom they regulate – but it would be very meaningful to the credit unions that are responsible for funding the activities of the agency. Similar hearings were held for several years until they were discontinued in 2009. Until such time that a law can be enacted to compel the agency to provide such a forum for credit union stakeholders, we encourage the Committee to ask the Chairman of the NCUA to testify annually on the agency's budget.

Improve the Structure of the CFPB to Achieve Better Results for Consumers and Covered Entities

Since it was first proposed, CUNA has tried to take a reasonable approach to the Consumer Financial Protection Bureau (CFPB). During the legislative process that resulted in the creation of the Bureau, we maintained that a consumer agency *could* be a good way to achieve important protections for consumers, particularly consumers of products and services provided by then-unregulated

entities. We also noted that credit unions did not in any way contribute to the financial debacle and their regulatory regime, coupled with their cooperative structure, protects against credit unions ever contributing to a financial crisis. We questioned the need for the Bureau's rules to apply to credit unions, for credit unions to be examined by the Bureau and for credit unions to have to pay for the operating expenses of the Bureau, because frankly, we didn't believe credit union members needed much protection from the credit unions that they own. And, we urged Congress to take steps to minimize the adverse impact the Bureau would have on credit unions' ability to serve their members.

We were encouraged by the authority included in the legislation for the Bureau to provide exemptions to its rules for entire classes of entities, like credit unions; and we hoped the Bureau would use this to focus its efforts on the wrongdoers and those that abuse consumers. Despite promises to "level the playing field" between regulated and unregulated financial product and service providers, this has not been the case and the impact of many of the CFPB's rules has been to make it more difficult for credit unions to fully serve their members. In fact, many credit unions have limited or eliminated certain financial products and services traditionally provided to their members as a direct result of the CFPB's rules. Five years after enactment, Congress should seriously consider structural changes at the Bureau to ensure that it meets its mission without jeopardizing the good work that credit unions do to serve their members.

Expand and Specify the CFPB's Exemption Authority

Section 1022 of Title X of the *Dodd-Frank Act* and a number of the enumerated consumer laws expressly authorize the Bureau to provide exemptions from the requirements of statutes or implementing regulations generally or the requirements of certain provisions specifically. These various statutory provisions individually and together grant broad authority to the Bureau and constitute a strong legal framework to support the agency's reasonable use of its exemption

authority. We believe that the Bureau should go much further than it has to exempt credit unions from its rule making, because credit unions, unlike other financial institutions, have not caused the abuse the Bureau is meant to address. The imposition of regulations designed to curb abuse elsewhere in the system reduces access to affordable products and services offered by credit unions. If the Bureau is unwilling to expand its perspective on the exemption authority that Congress has conveyed, Congress should state it more explicitly. We encourage the Committee to exercise significant oversight of the Bureau and press the agency on the impact its rules have on credit unions and their ability to provide their members access to credit and affordable financial products and services.

Install a Five-Person Board to Run the CFPB

CUNA encourages Congress to enact legislation to change the leadership structure at the Bureau from a single director to a five-person board. Expanding the Bureau's executive leadership to a five-person board will ensure that more voices contribute to the Bureau's rulemaking and it could help produce regulations that better balance the important mission of the Bureau and the impact the regulations have on the way products and services are provided to consumers.

We are not naïve: we know this is a highly politicized issue. Nevertheless, we encourage thoughtful consideration of this proposal now to ensure that the inaugural Board could be in place when Director Cordray's term expires, and we believe that the legislation could be developed so that the next president would nominate the initial Board members.

Fund the CFPB through the Appropriations Process

We renew our call on Congress to place the CFPB under the appropriations process in order to provide an additional layer of supervision over the activities of the Bureau. As you know, today, the Bureau is funded through transfers from the Federal Reserve Board of Governors. Subjecting the Bureau to the appropriations process would give Congress a powerful tool to help ensure that the activities of

the Bureau are consistent with its mission. Taking this step would help to ensure that the Bureau's rulemaking and supervisory activities do not harm consumers by making financial services less available and more expensive and do not erect unnecessary and overly burdensome barriers to credit unions and other providers of affordable financial products to consumers.

Substantially Increase the CFPB Examination Threshold

In July 2014, Senators Toomey (R-PA) and Donnelly (D-IN) introduced S. 2732, the *Consumer Financial Protection Bureau Examination and Reporting Threshold Act of 2014*. This legislation would have increased the threshold for examination of banks and credit unions by the CFPB from $10 billion to $50 billion.

Raising the threshold would provide significant regulatory relief to the affected institutions and direct Bureau resources to previously unregulated entities, as well as to the examination of the institutions that serve the greatest number of consumers. While this change would not significantly change the number of institutions and percentage of assets presently subject to examination by the Bureau, it would allow the Bureau to more efficiently use its examination resources in the coming years. The number of financial institutions approaching $10 billion in total assets is increasing. As these institutions cross the threshold, the Bureau will be required to spend more of its resources examining these newly covered institutions at the expense of other important consumer protection activities.

Institutions which would have been affected by S. 2732 would continue to be subject to the Bureau's rules and regulations, and they would be examined for compliance with these rules by their prudential regulator. In addition, Section 1026 of the *Dodd-Frank Act* provides the Bureau authority to examine on a sampling basis credit unions, thrifts and banks for which it does not have examination authority and includes language directing coordination between the prudential regulators and the Bureau.

While we support the legislation that was introduced, alternatively we would suggest the addition of language to index the threshold, at whatever level set, to the rate of inflation.

Require Cost-Benefit Analysis of all CFPB Proposals

We urge Congress to enact legislation to require the CFPB to complete an extensive cost-benefit analysis before the agency proposes a rule and to provide this analysis to the public with any proposal issued. The burden should be on the Bureau to detail the costs and benefits of its proposals, not on regulated parties to prove that there is a burden. We appreciated the focus that Chairman Shelby and others gave to this issue during the hearing with regulators earlier this week.

In the 113th Congress, Chairman Shelby introduced the *Financial Regulatory Responsibility Act* (S. 450) which would have required agencies to compare quantified benefits with quantified costs. The bill also would have required agencies to provide all data and analysis to the public (in the preamble of the rule) so that they can analyze the agencies' conclusions. Further, the legislation would have provided a mechanism for judicial review. We support the reintroduction of this legislation and encourage its enactment.

Codify the Credit Union Advisory Council

Shortly after the CFPB was established, the Bureau's leadership announced the creation of a credit union advisory council (CUAC). This group, which CUNA strongly supports, advises the agency on the impact of the Bureau's proposals on credit unions. CUAC shares information, analyses, recommendations and the unique perspective of not-for-profit financial institutions with the agency director and staff. However, since CUAC is not required by law, it could be abolished at any time. We believe CUAC is an important resource for the agency and also provides a forum for credit union officials to provide direct feedback to the agency on how proposals and final rules will affect credit unions' operations.

We ask Congress to codify the CFPB Credit Union Advisory Council as a legal requirement and to require the CFPB to reimburse all CUAC members for their travel and lodging expenses incurred to attend meetings of the CUAC.

Require Small Business Regulatory Enforcement Fairness Act Panels for CFPB Rulemakings

As required by the *Dodd-Frank Act*, the CFPB has held *Small Business Regulatory Enforcement Fairness Act* (SBREFA) panels for several of its regulations, including the mortgage rules. These panels, which are conducted under the auspices of the Small Business Administration's Office of Advocacy, are invaluable for identifying concerns and shedding light on costs small businesses, including credit unions, will have to bear under new proposals. However, the CFPB has taken the view that it is not required to hold a SBREFA panel for rulemakings that involve regulations transferred from other agencies, such as the international remittance transfers regulation that was initiated by the Federal Reserve Board. We ask Congress to direct the CFPB to hold SBREFA panels for all significant regulations that the CFPB promulgates.

Improve the Definition of "Rural and Underserved Areas"

The CFPB has taken steps to minimize the impact of its mortgage rules on certain small creditors, but these steps do not provide credit unions with sufficient relief because credit unions did not contribute to problem mortgages that fueled the financial crisis. We urge Congress to work with the CFPB to do much more to minimize the impact of the agency's rules on mortgage lending credit unions.

Currently, small creditors in rural and underserved areas can originate mortgage loans that exceed a debt-to-income ratio of 43% if the loans are held in portfolio, despite the qualified mortgage (QM) standards to the contrary. In addition, such creditors in rural or underserved areas can originate QMs with balloon payments, while other lenders may not under the QM provisions. Under the *Home Ownership and Equity Protection Act*, small creditors that operate

predominantly in rural or underserved areas are allowed to originate high-cost mortgages with balloon payments. Under the escrow rule, eligible small creditors do not have to set up escrow accounts for higher-priced mortgages.

The CFPB has recently issued a new proposal with changes to the agency's Escrow, Ability-to-Repay and *Home Ownership and Equity Protection Act* rules, several of which are intended to alleviate regulatory burdens imposed on small mortgage lenders serving rural or underserved areas. For example, the proposal would exempt creditors that originate up to 2,000 first-lien mortgage loans, as opposed to the current level of 500; loans held in portfolio also would not be included in determining mortgage-level activity for purposes of the exemption.

While these provisions are appreciated, they simply do not go far enough in light of the fact that credit unions were not the cause of the financial crisis and have not been engaging in abusive mortgage lending practices.

The CFPB is not proposing to raise the $2 billion assets threshold test for small creditors at this time even though the agency has the statutory authority to do so under the *Dodd-Frank Act*. The agency does index the threshold, which now stands at $2.060 billion as of December 2014. However, for purposes of mortgage lending, this threshold is far too low and we urge the agency to raise it to at least $10 billion, also indexed for inflation. This step would not harm consumers as community financial institutions, such as credit unions, work hard to ensure their borrowers can repay their loans and understand their terms. Such an increase would be consistent with the *Dodd-Frank Act's* treatment of smaller institutions that are not subject to the CFPB's direct examination authority. Also, it would provide important regulatory relief to key institutions that support our economy. We do not believe there is any good public policy reason to maintain the small creditor exemptions at such an artificially low level. We urge Congress to review the cut-off and work with the CFPB to increase the exemption level.

The proposal would enlarge the definition of "rural" areas to include census blocks that are not in an urban area as defined by the Census Bureau. CUNA supports efforts to expand the definition of rural but cautions that this approach may not be as easy to implement as the CFPB suggests, without easy-to-use resources. The Federal Communications Commission has provided a list of census blocks eligible for rural broadband support. We urge the CFPB to work with the Census Bureau to provide a list or direct-link to a list from the Census Bureau of rural census blocks for purposes of determining whether properties are located in rural areas.

We also have concerns with the CFPB's treatment of underserved areas. The pending proposal would conform provisions regarding "underserved areas" to the proposals mentioned above, but it is not seeking comments on the definition of underserved areas at this time.

Regulation Z provides that an area is "underserved" during a calendar year if, according to *Home Mortgage Disclosure Act* (HMDA) data, no more than two creditors extend covered transactions, as defined in § 1026.43(b)(1), secured by a first lien, five or more times in the county. We believe this approach is far too restrictive and we urge Congress to encourage efforts by the CFPB to develop a better, more inclusive definition of an underserved area that will benefit potential borrowers and communities that are underserved.

The CFPB is also proposing to cut the qualifying period for determining whether a creditor is operating predominately in a rural or underserved area from the three preceding calendar years to the preceding calendar year. CUNA opposes this proposed change.

Enact the Mortgage Choice Act

The QM rule sets the standard for consumer mortgages by providing significant compliance certainty to loans that do not have risky features and meet strict Federal requirements. A key requirement is that points and fees for a QM

generally may not exceed 3% of the loan amount. The problem arises from the fact that, under current law and rules, what constitutes a "fee" or a "point" towards the cap varies greatly depending upon who is making the loan and what arrangements are made by consumers to obtain title insurance. If the consumer chooses a title insurance provider that is affiliated with the lender, the title insurance charges count, but if the insurance is purchased from an unaffiliated title agency, the title charges do not count. In addition, escrowed homeowners insurance premiums may count as "points and fees" due to ambiguous drafting in the law.

We encourage Congress to enact legislation to exclude from the points and fees calculation affiliated title insurance charges and escrowed homeowners' insurance premiums. Without these amendments, the inclusion of title insurance and escrowed homeowners' premiums will cause many loans, especially those to low- and moderate-income consumers, to fail this prong of the QM test. As a result, many otherwise qualified borrowers will not get access to safe and affordable mortgage credit.

Raise the Points and Fees Limit on Qualified Mortgages Greater than $100,000

We encourage Congress to raise the points-and-fees limit on qualified mortgage loans greater than $100,000 from 3% to 4%. For a loan to be a QM, the points and fees may not exceed the points and fees caps. This is a statutory cap contained within section 129C of the *Truth in Lending Act* (TILA), as amended by section 1411 of the *Dodd-Frank Act*. The CFPB recognizes that the points and fees caps should be higher for smaller loans, and using its discretionary rulemaking authority, provides higher limits for loans less than or equal to $100,000.

This amendment is important to ensure credit availability to qualified consumers, especially those attempting to obtain mortgage credit in high-cost areas across the country. A higher fee limit on mortgage loans greater than

$100,000 will insure that fewer loans will be considered high cost mortgage loans subject to additional disclosures and limitations.

Standardize the Definition of Mortgage Originator

We encourage Congress to replace the definition of "mortgage originator" in the *Truth in Lending Act* with the *SAFE Act's* definition of "loan originator."

Under the *Dodd-Frank Act's* amendments to TILA, the term "mortgage originator" is overly broad and includes individuals who are not involved in the mortgage origination process, such as those who engage in advertising and promotional activities. On the other hand, the *SAFE Act's* definition provides an accurate representation of the limited duties a mortgage loan originator is required to perform, which are to take a residential mortgage loan application and offer or negotiate the terms of the residential mortgage loan for compensation or gain.

The definitions in both statutes should be aligned in order to reflect industry practice, facilitate the usage of standard terminology and definitions in the financial services industry's laws and regulations and reduce regulatory burden.

Deem Mortgages Held in Portfolio as Qualified Mortgages

We encourage Congress to amend the definition in Section 1412 of the *Dodd-Frank Act* to deem residential real estate mortgage loans made by credit unions and held in portfolio as "qualified mortgages."

This provision would help consumers have access to a wider array of loan products and terms. Credit unions and other financial institutions that hold residential mortgage loans on their balance sheets should generally have more flexibility in granting loans than financial institutions who make mortgage loans with the intention of selling them. Credit unions have demonstrated their responsible lending practices and have always adhered to the principle of ability-to-repay long before it was required by regulation. Credit unions enjoy low net charge off rates in their mortgage portfolios, which ultimately benefit consumers. Due to their

proven performance history, these loans should be afforded qualified mortgage status at the time of loan closing.

Enact Examination Fairness Legislation

Concerns regarding credit union examinations increase during difficult economic times, but even as the economy recovers, credit unions continue to express concern with their examinations. CUNA recently conducted a survey of credit unions regarding satisfaction with their most recent examination. [28] Twenty eight percent of credit unions reported dissatisfaction with their most recent exam. Excessive use of documents of resolution, applying "guidance" or "best practice" as if it was regulation, and examiners taking action to "cover" themselves stood out as the items that received the most negative ratings.

Credit unions support strong, fair and appropriate safety and soundness regulation and supervision to protect the financial resources of credit unions and their members and to minimize costs to the NCUSIF borne by all federally insured credit unions. Examinations should be based on the laws Congress enacts and the regulations that NCUA promulgates, not on examiner interpretation of "best practice" or guidance. Further, financial institutions need an examination appeals process that is independent and protects them from examiner retaliation.

In the last two Congresses, examination fairness legislation has been introduced. This legislation would have codified certain examination standards,

[28] CUNA/league affiliated credit unions received ongoing email correspondence from CUNA and their state league presidents inviting them to complete an on-line survey on their most recent exam. In addition, the survey was prominently featured on CUNA's website, in CUNA newsletters, and by leagues in a number of their communications with credit unions. The questionnaire was almost identical to one used in both 2012 and 2013. By September 10, 2014, we had received 447 responses, representing approximately 7% of all credit unions. On average, responding credit unions were once again somewhat larger than all US credit unions: For example, 37% of responding credit unions reported $25 millon or less in assets, while roughly 50% of all U.S. credit unions are this large. At the other end of the spectrum, 23% of responding credit unions have more than $250 million in assets compared to 11% of the population. In any case, there was strong response across all asset sizes. Because larger credit unions were more likely to respond, responses from single common bond credit unions were lower than the population, and community charters are more heavily represented. All totals reported in the survey will be weighted to the distribution of all credit unions by asset size when the final report is released, though doing so is unlikely to significantly change the observations found in this preliminary summary of findings.

provided an independent ombudsman to whom credit unions and banks could raise concerns about their exams and created an independent appeals process under which they could dispute determinations made in their exams. We would support the reintroduction of this legislation in the 114th Congress and encourage its enactment.

Address Issues Related to Federal Home Loan Bank Membership Eligibility

Ensure FHLB Membership Eligibility Rules are the Same for Small Credit Unions and Banks

We are very concerned about the September 2, 2014, proposal from FHFA to revise the agency's rules regarding membership in a Federal Home Loan Bank (FHLB). FHLBs are critical sources of liquidity for many credit unions, and the proposed regulation would make it much more difficult for both new and existing credit unions to maintain access to the FHLB system. CUNA questions the need for the proposal and submitted a comment letter to the agency on January 12, 2015, that asked the agency to withdraw the proposal.[29]

This proposed rule, which is based on an advance notice of proposed rulemaking (ANPR) issued almost four years ago, creates two core requirements for financial institutions. First, the rule would require all financial institutions who are FHLB members to hold one percent of their assets in "home mortgage loans" on an ongoing basis. The proposed regulation suggests that FHFA is considering raising this requirement to as high as five percent in the future. While financial institutions currently must meet the one percent-of-assets threshold to become

[29] Letter from Mary Mitchell Dunn, Deputy General Counsel, Credit Union National Association to Alfred Pollard, General Council, Federal Housing Finance Agency. Comments on Proposed Changes to Federal Home Loan Bank Membership Requirements/RIN 2590-AA39. January 12, 2015.
(http://www.cuna.org/uploadedFiles/CUNA/Legislative_And_Regulatory_Advocacy/Track_Regulatory_Issues/Pending_Regulatory_Changes/2014/FHLB_MembershipLetter_01122015.pdf)

FHLB members, there is no requirement at this time that the member maintain it to remain a member.

Second, all FHLB-member credit unions—but, because of a statutory limitation in the *Federal Home Loan Bank Act*, only certain banks—would also be required to hold 10% of assets in "residential mortgage loans" on an ongoing basis. By statute, for initial membership, the *Federal Home Loan Bank Act* exempts from the "10 percent" requirement any "community financial institution" or "CFI," as defined as FDIC-insured banks with less than $1 billion in average total assets (adjusted annually for inflation) over the preceding three years. Credit unions, generally insured by NCUA, are not eligible for this exemption. FHFA has proposed to maintain the "CFI" exemption without any variation for the purposes of *maintaining* membership, despite the fact that the agency has flexibility in this regard. FHFA should exercise its discretion and treat credit unions and banks equally if it moves forward with the proposal. CUNA also calls on Congress to amend the *Federal Home Loan Bank Act* to ensure credit unions are considered "community financial institutions" for the purpose of securing *initial* FHLB membership.

Beyond the issue of parity, we urge Congress to ask tough questions of FHFA regarding the need for this proposal as well as the details. Congress, not the regulator, should define who can be members of the FHLBs. FHFA is under no statutory obligation to impose these membership limits on an ongoing basis. Although we recognize FHFA has an interest in ensuring FHLB members maintain a commitment to housing finance, we believe this is a regulation in search of a problem. We are unaware of any financial institutions who can jump through the substantial regulatory hoops to become FHLB members, who are willing to buy stock in the FHLBs, and who meet the 10% requirement at the time of membership who are not committed to housing. This regulation will create another compliance task for credit unions, who will be forced to maintain a close watch over their

balance sheet to ensure they meet an arbitrary requirement on an ongoing basis. FHFA acknowledges that the proposed regulation will put the existing FHLB membership for some credit unions in jeopardy. Loss of FHLB membership will limit access to the low-cost source of funding provided by the FHLBs, restricting credit at a time when our nation's housing recovery remains fragile.

FHLB liquidity was a critical resource during the last financial crisis, and the proposed regulation would limit its utility in a future crisis. We hope FHFA will reconsider this proposal.

Make Privately Insured Credit Unions Eligible to Join the Federal Home Loan Bank System

We also support reintroduction of legislation that was introduced by Ranking Member Brown (D-OH) and Senator Portman (R-OH) last year to correct a drafting oversight in the *Federal Home Loan Bank Act* which has resulted in a small number of privately insured credit unions being ineligible to join a FHLB.

In 1989, in the wake of the savings and loan crisis, the FHLB System was opened up for the first time to commercial banks and credit unions. Unfortunately, the bill was drafted in such a way to apply only to an "insured credit union" as defined under the *Federal Credit Union Act*. If the legislation had used a broader term in the 12 USC 1752 of the *Federal Credit Union Act* – such as "state credit union" or "state-chartered credit union", terms that are clearly defined, then privately insured credit unions would have the same opportunity for membership as other financial institutions. This is why, for many years, we have suggested that this was likely an oversight in drafting. Unfortunately, it has meant for over two decades, a small group of credit unions have been denied the right to even apply for membership in the FHLB System.

The House of Representatives has continuously recognized this as a problem. In 2004, 2006 and 2014, the full House passed corrective legislation. In 2008, as part of the *Housing and Economic Recovery Act of 2008*, Congress made

a small change to permit privately-insured, state-chartered credit unions designated as a Community Development Financial Institution (CDFI) to apply for membership to the FHLBs; however, of the 127 privately insured credit unions, only two are CDFI certified.

We understand some policymakers have concerns regarding the existence of the private insurance option; however, this legislation would not expand that option for credit unions nor would it present an increased risk to the FHLB System, since this legislation only allows privately insured credit unions the option to apply for membership.

If enacted, privately insured credit unions would not be the only non-Federally insured institutions eligible for membership in the FHLB System. Currently, insurance companies, which are not federally insured, are members of the System. In fact, in terms of current outstanding advancements, 119 insurance companies are borrowing almost twice as much as 427 federally insured credit unions.[30]

It has never seemed reasonable to our small institutions that some of the largest banks in the world, insurance companies (which are not Federally insured) or a foreign bank's U.S. subsidiary can borrow billions of dollars from the FHLB System, but credit unions serving teachers in Ohio and Texas, firefighters in California, postal and county workers in Illinois and farmers in Indiana cannot.

Representatives Stivers (R-OH) and Beatty (D-OH) have introduced legislation in the House (H.R. 299) to address this issue. We look forward to the reintroduction of this legislation in the Senate and urge its enactment.

---

[30] According to the *Combined Financial Report of the Federal Home Loan Bank System for the Quarter ending on September 30, 2013.*

Enact the Privacy Notification Modernization Act

We encourage Congress to enact the *Privacy Notice Modernization Act* (S. 423), as introduced by Senators Moran (R-KS) and Heitkamp (D-ND), and cosponsored by Senators Crapo (R-ID), Tester (D-MT), Kirk (R-IL), Warner (D-VA), Corker (R-TN), Warren (D-MA), Heller (R-NV), Merkley (D-OR), Cotton (R-AR), Scott (R-SC) and Toomey (R-PA). This is an example of legislation that both reduces regulatory burden and improves consumer protection. The legislation would require financial institutions to send their customers privacy policy notifications only when the privacy policy is changed.

Under current law, financial institutions must send these notices on an annual basis regardless of whether the policy changes. This imposes a significant cost on credit unions and results in very little consumer benefit. Since 2001, credit unions have sent over 1 billion privacy notices to their members, averaging over 87,000,000 notices a year.

A voter survey conducted in 2013 showed that fewer than one-quarter of consumers read the privacy notifications they receive, and over three-quarters of consumers would be more likely to read them if they were only sent when the financial institution changed its policy. This suggests that the public policy goal of privacy notifications would be better achieved if the notices had more meaning to consumers. We believe that this legislation achieves this goal.

The legislation has passed the House of Representatives on a number of occasions, most recently in March 2013. The Senate bill in the last session enjoyed the co-sponsorship of 74 Senators. This is common sense legislation that should be enacted quickly.

Stop Merchant Data Breaches

Credit unions are subject to high data protection standards under the *Gramm-Leach-Bliley Act,* and they take their responsibility to protect their

members' data seriously. Unfortunately, there is a weak link in the payments system that leaves consumers' financial data vulnerable to theft by domestic and international wrongdoers. The weak link is the absence of Federal data security standards for the merchants that accept payment cards.

There have been several very high profile merchant data breaches in the last few years, notably the breaches at Target in 2013 and Home Depot in 2014. Millions of credit union members were affected by these two breaches, which ultimately cost credit unions – and by extension their members – nearly $100 million. Despite the recovery efforts of payment card networks, no credit union has received a dime from the merchants whose security failure allowed the breach. Credit unions and their members are left on the hook.

These two breaches made headlines, but merchant data breach is a chronic issue. The endless string of breaches demonstrates clearly that those who accept payment cards need to be subject to the same Federal data standards as those who issue the cards.

It is important to recognize that the costs of a merchant data breach scenario on a small financial institution will be relatively greater than the costs of the same breach on large financial intuitions. For example, credit unions do not enjoy the economies of scale that national megabanks do. Therefore, the cost of everything, from replacing a debit card to monitoring suspicious activities, is greater.

Credit unions join with our colleagues in the banking industry to call on Congress to enact meaningful data security legislation that incorporates the following principles:

- Strong national data protection and consumer notification standards with effective enforcement provisions must be part of any

comprehensive data security regime, applicable to any party with access to important consumer financial information.

- Banks and credit unions are already subject to robust data protection and notification standards. These *Gramm-Leach-Bliley Act* requirements must be recognized.
- Inconsistent state laws and regulations should be preempted in favor of strong Federal data protection and notification standards.
- In the event of a breach, the public should be informed where it occurred as soon as reasonably possible to allow consumers to protect themselves from fraud. Banks and credit unions, which often have the most direct relationship with affected consumers, should be able to inform their customers and members about the breach, including the entity at which the breach occurred.
- Too often, banks and credit unions bear a disproportionate burden in covering the costs of breaches occurring beyond their premises. All parties must share in protecting consumers. Therefore, the costs of a data breach should ultimately be borne by the entity that incurs the breach.

There are a number of Congressional committees exploring remedies to merchant data breaches. Given the very direct and detrimental impact these breaches have on credit unions and banks, we ask the Committee to take a strong leadership role in these efforts.

Vendor Authority

We are deeply concerned that NCUA continues to urge Congress to convey to the agency supervisory authority over vendors and credit union service

organizations (CUSOs). Further, we are troubled by their recent assertion that having such authority would represent regulatory relief for credit unions.[31]

Credit unions are already supervised for due diligence in third-party vendor relationships during their regular examinations. Giving NCUA additional authority to supervise third party vendors would increase the cost of the services these entities provide credit unions without providing any added benefit to the agency. We are also unconvinced that NCUA needs authority to regulate CUSOs inasmuch as CUSOs are generally owned by credit unions, subject to a statutory restriction that guards against concentration risk. The *Federal Credit Union Act* limits investment in a CUSO to 1% of a Federal credit union's total assets. We encourage the Committee to reject NCUA's request for additional supervisory authority.

Interest Rate Risk

As part of its risk-based capital proposal, NCUA provided advance notice that it intends to consider a new proposal related to interest rate risk. While we will provide greater detail in our comment letter, we question whether a new rule on interest rate risk is necessary given the fact that NCUA presently has many supervisory tools that could be used to identify unreasonable interest rate risk at individual credit unions. We ask the Committee to explore with the agency whether a new rule is necessary or whether this might be better monitored through improvements in the supervisory process.

Conclusion

The length of this testimony and the breadth of the issues discussed herein are an indicator of just how many barriers credit unions face as they work to fulfill the mission that Congress has given them. We are confident that if barriers are removed, credit union members will be better off than they are today, because their

[31] Fazio. 15.

credit unions will be spending less resources on complying with outdated, poorly focused and unreasonably burdensome regulation, and more on meeting the financial services needs of their members. We stand ready to work with you to remove these barriers.

On behalf of America's 6,500 credit unions and their 102 million members, thank you very much for the invitation to testify at today's hearing.

CUNA
Credit Union National Association

601 Pennsylvania Ave., NW
South Building, Suite 600
Washington D.C. 20004-2601

Phone: 202-638-5777
Fax: 202-638-7734

Finalized Federal Regulatory Changes Applicable to Credit Unions (Effective Dates on or after January 1, 2008)[32]

	Effective Date	Agency	Title of Final Rule	Pages in Federal Register
1	1/1/2008	FEMA	FEMA Flood Map Changes	2
2	1/1/2008	IRS	Annual Electronic Filing Requirement For Small Tax Exempt Organizations – Form 990-N	1
3	1/1/2008	IRS	IRS Form 990 Instructions - New Reporting Form	79
4	1/1/2008	IRS	IRS Redesign Form 990	28
5	5/29/2008	NCUA	Disclosures for Subprime Mortgage Loans	9
6	7/7/2008	FTC	CAN-SPAM Act Rules	27
7	10/1/2008	FHA	Hope for Homeowners Program for Subordinate Lienholders	6
8	10/10/2008	FASB	Use of Fair Value in an Inactive Market	7
9	10/22/2008	NCUA	Share Insurance Signs to Reflect Increased Limits	2
10	10/31/2008	NCUA	Official Advertising Statement	2
11	11/21/2008	NCUA	Incidental Powers	7

[32] Last updated: February 2015

12	12/15/2008	FASB	Amendments to the Impairment Guidance No. 99-20	44
13	12/31/2008	NCUA	PCA: Amended Definition of Post-Merger Net Worth	4
14	1/2/2009	NCUA	Criteria to Approve Service to Underserved Areas	5
15	1/7/2009	FHA	Interim Final Rule on Hope for Homeowners Program	6
16	1/16/2009	HUD	Final RESPA Rule	85
17	1/19/2009	FED	Unlawful Internet Gambling	31
18	4/3/2009	NCUA	Share Insurance Signs for Shared Branching	3
19	4/27/2009	NCUA	RegFlex Changes for Unimproved Land	1
20	5/14/2009	NCUA	Technical Changes to the FACT Act "Red Flags"	8
21	6/15/2009	FASB	Fair Value: Decrease in Market Activity/Transactions That Are Not Orderly	27
22	6/15/2009	FASB	Recognition and Presentation of Other-Than-Temporary Impairments	64
23	6/20/2009	FED	Restructuring of Fed's Check Processing : Districts 10, 11, and 12	2
24	7/2/2009	FED	Fed Rule Authorizing Excess Balance Accounts and Earnings on Balances	10
25	7/2/2009	FED	Fed Rule Authorizing Pass-through Accounts and Adjusting the Limitation on Savings Account Transfers	11
26	7/19/2009	FED	Restructuring of Federal Reserve's Check Processing : Districts 6 and 8	2
27	7/25/2009	FED	Restructuring of Federal Reserve's Check Processing : Districts 4 and 9	2
28	7/30/2009	FED	Revisions to Regulation Z Mortgage Loan Disclosures	17
29	9/1/2009	NCUA	Credit Union Reporting	3

30	9/12/2009	FED	Restructuring of Federal Reserve's Check Processing : Districts 4 and 7	2
31	9/14/2009	FED	Regulation Z Disclosures for Private Student Loans	63
32	9/21/2009	FED	Regulation Z Rule Implementing the CARD Act	26
33	10/1/2009	FED	Amendments to the Home Mortgage Provisions of Regulation Z	93
34	10/17/2009	FED	Restructuring of Federal Reserve's Check Processing : Districts 11 and 12	3
35	10/18/2009	FED	Restructuring of Federal Reserve's Check Processing : District 4	3
36	10/18/2009	FED	Restructuring of Federal Reserve's Check Processing : District 6	3
37	11/6/2009	FHFA	Election of Federal Home Loan Bank Directors	13
38	11/14/2009	FED	Restructuring of Federal Reserve's Check Processing : Districts 11 and 12	3
39	11/30/2009	NCUA	Share Insurance Coverage for Revocable Trust Accounts	9
40	11/30/2009	NCUA	Temporary Increase in SMSIA; Display of Official Sign; Coverage for Mortgage Servicing Accounts	10
41	12/12/2009	FED	Restructuring of Federal Reserve's Check Processing : District 3	2
42	12/24/2009	NCUA	Exceptions to the Maturity Limit on Second Mortgages	2
43	1/1/2010	FED	Overdraft Protection Disclosures	11
44	1/1/2010	FED	Revisions to Regulation S	4
45	1/1/2010	NCUA	Operating Fees	3
46	1/1/2010	NCUA	Truth in Savings Rule for Overdraft Protection and Electronic Disclosures	5

47	1/4/2010	NCUA	NCUSIF Premium and One Percent Deposit	7
48	2/4/2010	FHFA	Federal Home Loan Bank Membership to Include Non-Federally Insured CDFI Credit Unions	27
49	2/10/2010	FinCEN	Expansion of Special Information Sharing Procedures To Deter Money Laundering and Terrorist Activity	11
50	2/14/2010	FED	Regulation Z Disclosures for Private Student Loans	63
51	2/22/2010	FED	Regulation Z Rule Implementing the CARD Act	268
52	2/27/2010	FED	Consolidation of Federal Reserve's Check-Processing	2
53	5/21/2010	NCUA	Interagency Policy Statement on Funding & Liquidity Risk Management	11
54	6/4/2010	FED	Establishment of Term Deposits at Federal Reserve Bank	6
55	6/18/2010	NACHA	Direct Access Registration Requirement	6
56	6/18/2010	NACHA	Risk Management and Assessment	4
57	7/1/2010	Education	Final Rules for Student Loans	35
58	7/1/2010	FED	Regulation Z Open-end Credit Final Rule	255
59	7/1/2010	FED	Regulation E Final Rule for Overdraft Protection Plans	8
60	7/1/2010	FTC	FACT Act Rules and Guidelines on the Accuracy of Credit Information	87
61	7/1/2010	NCUA	FACT Act Rules and Guidelines on the Accuracy of Credit Information	45
62	7/1/2010	NCUA	NCUA Final Rule on Unfair and Deceptive Practices for Credit Cards	3
63	7/6/2010	FTC	Disclosures for Non-federally Insured Credit Unions	7
64	7/26/2010	NCUA	Chartering and Field of Membership (FOM): Federal Credit Unions	9

65	8/2/2010	FED	FedACH SameDay Service	3
66	8/5/2010	NCUA	Low-Income Definition	2
67	8/16/2010	IRS	Payments Made in Settlement of Payment Card and Third-Party Network Transactions	16
68	8/22/2010	FED	Final Rule Implementing the CARD Act Provisions for Penalty Fees and Rate Reviews	68
69	8/22/2010	FED	Regulation E Rules for Gift Cards	43
70	9/2/2010	NCUA	Display of Official Sign; Permanent Increase in Standard Maximum Share Insurance Amount	3
71	9/7/2010	FED	Clarifications of Reg E and Reg DD Overdraft Rules	4
72	9/7/2010	NCUA	Clarifications on Reg DD Overdraft Protection Rules	4
73	10/1/2010	NCUA	SAFE Act	54
74	10/4/2010	HUD	FHA Risk Reduction Final Rule	4
75	10/18/2010	NCUA	Reverse Mortgage Guidance	12
76	10/25/2010	NCUA	Short-Term, Small Amount Loans	6
77	11/29/2010	NCUA	RegFlex Program Changes	4
78	11/29/2010	FED	Extension of CARD Act Effective Date for Gift Cards	5
79	12/23/2010	NCUA	Conversions of Insured CUs: Definition of Regional Director	2
80	12/31/2010	NCUA	Model Privacy Notices	105
81	1/1/2011	FED	FACT Act Risk-Based Notice Rule	61
82	1/1/2011	FED	Consumer Notification of Mortgage Loan Sales or Transfers	16
83	1/1/2011	FTC	Notice Regarding Charges Permitted Under the FCRA	1

84	1/1/2011	NACHA	Mobile ACH Payments	1
85	1/3/2011	FinCEN	Confidentiality of Suspicious Activity Reports	15
86	1/18/2011	NCUA	Corporate Credit Union Rule	4
87	1/20/2011	NCUA	IRPS 11-1 Supervisory Review Committee	4
88	1/27/2011	NCUA	Fiduciary Duties at Federal Credit Unions, and Mergers and Conversions of Insured Credit Unions	18
89	1/30/2011	FED	Interim Final Rule on Disclosures Required under the Mortgage Disclosure Improvement Act	8
90	1/31/2011	FED	Extension of CARD Act Gift Card Rules	1
91	3/14/2011	NCUA	Conversions of Insured Credit Unions: Definition of Regional Director	1
92	3/23/2011	NCUA	Corporate Credit Unions: Technical Corrections	1
93	3/23/2011	NCUA	PCA: Amended Definition of "Low-Risk Assets	2
94	3/24/2011	Treasury	Garnishment of Accounts Containing Federal Benefit Payments	24
95	3/28/2011	FinCEN	Amendment to BSA Regulations: Reports of Foreign Financial Accounts	1
96	3/28/2011	NCUA	IRPS: Chartering Corporate Federal Credit Unions	4
97	4/1/2011	FED	Interim Final Rule on Appraisal Independence	35
98	4/1/2011	FED	Loan Compensation and "Steering" of Loans	30
99	4/4/2011	FHA	Temporary Minimum Capital Increase for FHFA Regulated Entities	7
100	6/24/2011	NCUA	Technical Correction - Golden Parachute and Indemnification Payments	2
101	6/24/2011	NCUA	Temporary Unlimited Share Insurance for Noninterest-bearing Transaction Accounts	3

102	6/27/2011	NCUA	Golden Parachute and Indemnification Payments	12
103	7/21/2011	CFPB	Consumer Financial Rules to be Enforced by the CFPB	2
104	7/22/2011	CFPB	Regulation D Interim-Final Rule Implementing the Alternative Mortgage Transaction Parity Act	19
105	7/25/2011	NCUA	Sample Income Data to Meet the Low-income Definition	3
106	7/27/2011	NCUA	Remittance Transfers Interim Final Rule	2
107	8/10/2011	HUD	Technical Corrections & Clarifying Amendments to RESPA Regulations	4
108	8/15/2011	FED	Fair Credit Reporting Risk-Based Pricing (Credit Score Disclosures)	24
109	8/15/2011	FED	Regulation B - Equal Credit Opportunity Act (Credit Score Disclosures)	13
110	8/19/2011	FTC	Mortgage Acts & Practices - Advertising Rule	22
111	8/29/2011	HUD	SAFE Mortgage Licensing Act: Minimum Licensing Standards and Oversight Responsibilities	38
112	10/1/2011	FED	CARD Act Clarifications	93
113	10/1/2011	FED	Debit Interchange Fee and Routing Regulations (Regulation II)	82
114	10/1/2011	FED	Federal Reserve Board's Interim Final Rule on the Interchange Fee Fraud-Prevention Adjustment	11
115	10/19/2011	Treasury	Indorsement and Payment of Checks Drawn on the United States Treasury	3
116	10/31/2011	NCUA	Net Worth & Equity Ratio	4
117	11/14/2011	Labor	Notification of Employee Rights under the National Labor Relations Act	44
118	11/30/2011	NCUA	NCUA Remittance Transfers Rule	2

119	12/2/2011	NCUA	Community Development Revolving Loan Fund (CDRLF) Access for Credit Unions	8
120	12/23/2011	NCUA	Low-Income Designation – Technical Amendment	1
121	1/1/2012	NCUA	Accuracy of Advertising and Notice of Insured Status	2
122	1/23/2012	NCUA	Corporate Credit Union Rule – Technical Amendment	3
123	4/19/2012	IRS	Guidance on Reporting Interest Paid to Nonresident Aliens	5
124	5/31/2012	NCUA	Corporate Credit Union Follow-up Rule	10
125	6/29/2012	CFPB	Rules of Practice for Adjudication Proceedings	44
126	6/29/2012	CFPB	Rules Relating to Investigations Final Rule	11
127	7/2/2012	NCUA	Regulatory Flexibility Program	12
128	7/2/2012	NCUA	Regulatory and Reporting Treatment of Troubled Debt Restructurings	12
129	7/12/2012	FED	Regulation J (Collection of Checks and Other Items by Federal Reserve Banks, Etc)	7
130	7/12/2012	FED	Regulation D (Reserve Requirements of Depository Institutions: Reserves Simplification)	8
131	8/16/2012	CFPB	Confidential Treatment of Privileged Information Final Rule	7
132	9/17/2012	CFTC	End-User Exemption to the Mandatory Clearing of Swaps	32
133	9/30/2012	NCUA	Interest Rate Risk Policy and Program Final Rule	12
134	10/1/2012	FED	Debit Interchange Fee and Routing Regulations (Regulation II) -Fraud	25
135	11/23/2012	CFPB	Delayed Implementation of Certain New Mortgage Disclosures	9
136	11/30/2012	FED	Reserve Requirements of Depository Institutions	2

137	12/13/2012	NCUA	Fidelity Bond	2
138	12/15/2012	FASB	Guidance on Troubled Debt Restructurings	27
139	1/18/2013	NCUA	Treasury Tax and Loan Depositaries; Depositaries and Financial Agents of the Government Final Rule	1
140	2/19/2013	NCUA	Acceptance Deadline - Low-Income Designation Final Rule	2
141	2/19/2013	NCUA	Definition of a "Small Credit Union" Final Rule	6
142	2/19/2013	NCUA	Definition of "Troubled Condition" Final Rule	3
143	3/18/2013	FHA	Implementation of the Fair Housing Act's Discriminatory Effects Standard Final Rule	23
144	3/26/2013	CFPB	Disclosures at Automated Teller Machines Final Rule - Reg E	4
145	3/28/2013	CFPB	Credit Card Limitations on Fees Final Rule - Reg Z	4
146	3/29/2013	NCUA	Investment and Deposit Activities (TIPS) Final Rule	2
147	4/1/2013	NCUA	Rural District Final Rule	3
148	5/31/2013	NCUA	Technical Amendments Final Rule	6
149	6/1/2013	CFPB	Escrow Accounts Final Rule - Reg Z	32
150	6/1/2013	CFPB	Escrow Accounts Amendments Final Rule - Reg Z	8
151	6/11/2013	NCUA	Alternatives to the Use of Credit Ratings Final Rule	9
152	6/28/2013	FMS	Garnishment of Accounts Containing Federal Benefits Final Rule	12
153	7/1/2013	FTC	COPPA Final Rule	43
154	7/25/2013	NCUA	Loan Participations Final Rule	12
155	10/28/2013	CFPB	Remittance Transfers 2012 Final Rule - Reg E	117

156	10/28/2013	CFPB	Remittance Transfers Safe Harbor, Preauthorized Transfers Final Rule - Reg E	46
157	10/28/2013	CFPB	Remittance Transfers 2013 Final Rule - Reg E	61
158	11/18/2013	NCUA	Federal Credit Union Ownership of Fixed Assets Final Rule	4
159	11/4/2013	CFPB	Consumer's Independent Ability to Pay Final Rule - Reg Z	22
160	12/19/2013	NCUA	Charitable Donation Accounts Final Rule	3
161	1/1/2014	NCUA	Electronic Filing of Financial and Other Reports Final Rule	2
162	1/3/2014	FinCEN	BSA Definitions - Definitions of Transmittal of Funds and Funds Transfer Final Rule	4
163	1/10/2014	CFPB	Mortgage Loan Origination Compensation Final Rule	148
164	1/10/2014	CFPB	Mortgage Servicing Final Rule - Reg X	203
165	1/10/2014	CFPB	Mortgage Servicing Final Rule - Reg Z	120
166	1/10/2014	CFPB	Ability to Repay / QM Final Rule	213
167	1/10/2014	CFPB	Ability to Repay / QM - Exemptions, Modifications, and Clarifications	15
168	1/10/2014	CFPB	QM and Mortgage Servicing Clarifications	42
169	1/10/2014	CFPB	HOEPA – "High-Cost Mortgage" Loans Final Rule	120
170	1/10/2014	CFPB	Homeownership Counseling Organizations Lists Interpretive Rule	2
171	1/18/2014	CFPB	Regulation B - Copies of Appraisals Final Rule	35
172	1/18/2014	NCUA	Interagency Higher-Priced Mortgage Appraisals Final Rule	80
173	1/18/2014	NCUA	Interagency Higher-Priced Mortgage Appraisals Supplemental Final Rule	69

174	3/3/2014	NCUA	Derivatives Final Rule	19
175	3/31/2014	NCUA	Liquidity and Contingency Funding Plans Final Rule	4
176	5/30/2014	NCUA	Capital Planning and Stress Testing	7
177	7/1/2014	IRS	FATCA- (Temporary Regulations under Chapter 4)	54
178	7/1/2014	IRS	FATCA - (Temporary Regulations under Chapters 3 and 61)	84
179	6/30/2014	NCUA	Credit Union Service Organizations (CUSOs) Final Rule	13
180	7/1/2014	IRS	FATCA Final Rule	123
181	7/17/2014	CFPB	Application of Regulation Z's Ability-to-Repay Rule to Certain Situations Involving Successors-in-Interest	3
182	7/17/2014	CFPB	Policy Guidance on Supervisory and Enforcement Considerations Relevant to Mortgage Brokers Transitioning to Mini-Correspondent Lenders	5
183	7/28/2014	NCUA	Voluntary Liquidation Final Rule	3
184	10/3/2014	NCUA	Unfair or Deceptive Acts or Practices; Technical Amendments	4
185	10/23/2014	CFPB	Compliance Bulletin and Policy Guidance—Mortgage Servicing Transfers	5
186	10/28/2014	CFPB	Annual Privacy Notice Requirement Under the Gramm-Leach-Bliley Act (Regulation P)	26
187	11/17/2014	CFPB	Electronic Fund Transfers (Regulation E) (Remittances Temporary Exception)	26
188	1/10/2015	HUD	Federal Housing Administration (FHA): Adjustable Rate Mortgage Notification Requirements and Look-Back Period for FHA-Insured Single Family Mortgages	3
189	1/20/2015	NCUA	Appraisals; Appraisals; Availability to Applicants & Requirements for Transactions on Existing Extension of Credit	3

190	1/21/2015	HUD	Federal Housing Administration (FHA): Handling Prepayments: Eliminating Post-Payment Interest Charges	4
191	8/1/2015	CFPB	Integrated Mortgage Disclosures under TILA and RESPA Final Rule	1273
			Total Pages:	**5930**

INDEPENDENT COMMUNITY
BANKERS *of* AMERICA

Testimony of

John Buhrmaster
President & CEO
Of
First National Bank of Scotia
Scotia, NY

On behalf of the
Independent Community Bankers of America

Before the

United States Senate
Committee on Banking, Housing, and Urban Affairs

Hearing on

"Regulatory Relief for Community Banks and Credit Unions"

February 12, 2015
Washington, D.C.

Chairman Shelby, Ranking Member Brown, and members of the Committee, my name is John H. Buhrmaster, and I am President and CEO of First National Bank of Scotia, a $425 million asset bank in Scotia, New York. I am also Chairman of the Independent Community Bankers of America and testify today on behalf of more than 6,500 community banks nationwide. Thank you for convening today's hearing on "Regulatory Relief for Community Banks and Credit Unions."

The 114th Congress provides a unique opportunity to provide meaningful regulatory relief for community banks. What's at stake is the future of the American banking industry. Do we want a system with fewer, larger megabanks, more systemic risk, less consumer choice, and commodified product offerings? Should large swathes of rural and small town America be deprived of access to essential banking services to support their prosperity? Small town America is built on community bank credit. The rich tradition of community banking – built on personal relationships, customized offerings, and local decision making – is at risk today because of regulatory overkill grossly out of proportion to any systemic or consumer risk posed by community banks.

A community bank is not simply a megabank on a smaller scale. A community bank is distinct from a megabank in its simplified business model, traditional products and services, and community-orientated character. The fundamental financial policy error of recent years has been applying monolithic regulatory mandates to community banks without recognition of these critical differences. Meaningful regulatory relief is critical to sustaining community bank prosperity and independence which supports the economic vitality of the thousands of communities served primarily by community banks. Such relief is needed in the short term, not medium term or the long term. I urge this committee not to let this opportunity slip.

ICBA's regulatory relief agenda is embodied in our newly released "Plan for Prosperity for the 114th Congress," which I will describe in this testimony. But at the outset, I would like to thank the members of this committee for their efforts and leadership in the adoption of H.R. 3329 at the end of the 113th Congress, which raised the qualifying asset threshold under the Federal Reserve's Small Bank Holding Company Policy Statement from $500 million to $1 billion. This law will provide significant relief for nearly 650 bank holding companies. I asked for this, on behalf of community bankers, in my testimony before this Committee last September, and you delivered. Already in the 114th Congress, you passed an amendment to the Terrorism Risk Insurance Act to ensure community bank representation on the Federal Reserve Board of Governors. That too is now law. On behalf of my bank and all community banks, thank you. You've earned our gratitude.

In addition to the ICBA's Plan for Prosperity (attached), my testimony will be dedicated to legislation that, with this Committee's support, will be appropriately deliberated and vetted in the 114th Congress. Before getting to that, let me note another legislative issue already backed by broad consensus and ripe for enactment: privacy notice relief. The Privacy Notice Modernization Act from the 113th Congress (S. 635), sponsored by Senators Sherrod Brown (D-OH) and Jerry Moran (R-KS), had more than 70 cosponsors.

A similar bill passed the House under suspension. ICBA urges the Committee's assistance in obtaining swift passage of legislation to provide relief from annual privacy notice mailings when a bank has not changed its privacy policies. These notices are a source of confusion: customers who receive the annual notice often assume our policies have changed when they have not.

America's community banks are critical to the prosperity of the U.S. economy, particularly in small and rural communities. As the FDIC Community Banking Study showed, in one out of every five counties in the United States, the only physical banking presence is offices operated by community banks.[1] Community banks provide 60 percent of all small business loans under $1 million and 77 percent of agricultural loans, according to a newly released study from Harvard's Kennedy School.[2] Agricultural lending in particular is a very specialized form of lending that requires extensive knowledge of farming, crops, and local conditions.[3] This form of credit simply cannot be duplicated by larger banks that operate from outside the community. Community banks also offer customized mortgages suited to the unique characteristics of their local communities, while experiencing lower default rates than larger banks. Well capitalized with an average Tier 1 ratio of 10.5 percent,[4] community banks are playing a vital role in ensuring the economic recovery is robust and broad-based, reaching communities of all sizes and in every region of the country.

First National Bank of Scotia serves rural and suburban communities in the area of Albany, Schenectady, and Saratoga in upstate New York. We are a closely-held bank, employing 140 people and offering a full range of traditional banking services. First National Bank of Scotia has served these communities since 1923 and I'm a fourth generation community banker. Our story, our culture of relationship banking, and the role we play in our communities are typical of thousands of community banks.

The onerous regulatory burden on community banks is growing both in volume and complexity, suffocating the true potential of community banks to spur economic growth and job creation in their communities. My compliance officers have documented 153 final regulations, from a spectrum of federal agencies, implemented since 2007. These final regulations run the gamut from Bank Secrecy Act to credit card regulation to the multiple code sections that govern mortgage lending and servicing. In addition, there are 87 compliance changes in the form of guidance and statements and 59 annual adjustments to thresholds, lists of communities, and other data needed to maintain compliance. During that time period, more than 103 proposed regulations were issued which need to be reviewed as well. While not all of these changes apply to my bank, we nonetheless have to evaluate each one to determine to what extent our organization is impacted. Every change requires software updates, a lengthy process that includes a risk

---

[1] FDIC Community Banking Study. December 2012.

[2] "The State and Fate of Community Banking." Marshall Lux and Robert Greene. Mossavar-Rahmani Center for Business and Government at the Harvard Kennedy School. February 2015.

[3] Ibid.

[4] Esther George, President, Federal Reserve Bank of Kansas City (speech at the Community Banking in the 21st Century conference, Federal Reserve System & Conference of State Bank Supervisors, St. Louis, Mo., September 2014. Quoted in Lux and Greene.

assessment, installation on a test network, testing, installation on a production network, more testing, procedural review, training and audit. What's more, policy revisions require committee review and Board approval. Compliance changes result in legal and audit expenses and sometimes the expense of printing and mailing new disclosures. But most significant is the drain on staff time. Banks the size of First National Bank of Scotia, in contrast to the larger banks, do not have dedicated compliance departments. We have to divert valuable staff from other duties, including serving customers, to implement new rules and other changes, a process that can take weeks or months depending on the complexity of the change and the bank processes impacted. On behalf of all community bankers, I appeal to you for relief from the volume and complexity of regulation that is threatening the viability of the community bank business model.

The experience of First National Bank of Scotia is typical of community banks, as confirmed by ICBA's 2014 Community Bank Lending Survey (Survey) which surveyed over 500 community banks nationwide. Seventy-eight percent of respondents reported they had increased the number of staff dedicated to lending compliance in the past five years. In a lightly staffed community bank, any additional hiring is significant. Hiring dedicated to compliance, rather than serving customers, is a deadweight loss that diverts resources from community lending. I will share more results from the Survey later in this testimony. Let me just say here the survey clearly illustrated the negative impact new rules are having on credit availability and consumer choice. An Executive Summary of the Survey and Infographic are attached to this statement.

Working with community bankers from across the nation, ICBA developed its Plan for Prosperity for the 114th Congress, a platform of legislative recommendations that will provide meaningful relief for community banks and allow them to thrive by doing what they do best – serving and growing their communities. Each provision of the Plan was crafted to preserve an strengthen consumer protections and safety and soundness.

In this testimony, I will describe the major elements of the Plan and note examples of legislation that embodies Plan provisions. In the 113th Congress, more than 20 such bills were introduced in the House and the Senate. These bills, most of which enjoyed strong bipartisan support, set the stage for action in the 114th Congress. A complete listing of Plan for Prosperit bills introduced in the 113th Congress and their progress is attached to this testimony.

The Plan is organized around three broad themes: relief from mortgage regulation to promote lending, improved access to capital to sustain community bank independence, and reforming oversight and examination practices to better target the true sources of financial sector risk.

Mortgage Reform for Community Banks

Every aspect of mortgage lending is subject to new, complex, and expensive regulations that are upending the economics of this line of business. In ICBA's recent Community Bank Lending Survey, 44 percent of respondents said they made fewer first lien residential mortgage loans in 2014 when the CFPB's qualified mortgage rules were in

effect than they made in 2013. In a strengthening housing market, more banks should have been making more loans. More troubling, 73 percent of respondents said regulatory burdens were preventing them from making more residential mortgage loans.

Key provisions of the Plan for Prosperity are designed to keep community banks in the business of mortgage lending. ICBA was very pleased that two Plan for Prosperity mortgage provisions were included in the **Community Lending Enhancement and Regulatory Relief Act of 2013 (the CLEAR Relief Act, S. 1349)**. The CLEAR Act, sponsored by Sens. Jerry Moran (R-KS), Jon Tester (D-MT), and Mark Kirk (R-IL), was the Senate bill that best represented the scope of the Plan for Prosperity in the last Congress. With more than 40 bipartisan cosponsors, the bill represented a set of genuinely consensus solutions to ensure continued access to consumer credit and other banking services. We are grateful to the members of this committee that sponsored and cosponsored the CLEAR Act. The bill's mortgage provisions were:

- "Qualified mortgage" status under the CFPB's ability-to-repay rules for any mortgage originated and held in portfolio for at least three years by a lender with less than $10 billion in assets.
- An exemption from any escrow requirements for any first lien mortgage held in portfolio by a lender with less than $10 billion in assets.

The principal rationale for these provisions, and the reason they can be safely enacted, is they apply only to loans originated and held in portfolio by community banks. QM defines mortgages that are either "conclusively" or "presumptively" deemed to comply with the Dodd-Frank Act "ability-to-repay" requirements. As relationship lenders, community bankers are in the business of knowing their borrowers and assessing their ability to repay a loan. What's more, when a community bank holds a loan in portfolio it holds 100 percent of the credit risk and has an overriding incentive to ensure the loan is well underwritten and affordable to the borrower. In a typical community bank portfolio, even a small number of defaults can put a bank at risk. Community bank portfolio lenders ensure they understand the borrower's financial condition and structure the loan accordingly. If the borrower has trouble making payments due to job loss or other unforeseen circumstances, a community bank portfolio lender will work with the borrower to restructure the loan and keep the borrower in their home. By the same token, portfolio lenders will protect their collateral by ensuring borrowers remain current on tax and insurance payments. For this reason, the escrow requirement, which must be outsourced at a relatively high cost by community banks with a low volume of mortgages, is an unnecessary burden when a loan is held in portfolio. ICBA supports the CFPB's recent proposed rule that would expand the definitions of "small creditor" and "rural area." A "small creditor" mortgage held in portfolio may obtain QM status without regard to the 43 percent debt-to-income test. A small creditor that lends predominantly in rural or underserved areas can obtain QM status for balloon loans held in portfolio. However, ICBA urges Congress to revise the statute and pave the way for additional relief from the complex new mortgage rules by granting QM status to all portfolio loans held by community banks with up to $10 billion in assets. This will help ensure access to community bank mortgage credit.

The Plan for Prosperity contains additional mortgage provisions that were embodied in House legislation introduced in the last Congress. The **Community Bank Mortgage Servicing Asset Capital Requirements Study Act (H.R. 4042)** would have provided relief from the punitive capital treatment of mortgage servicing assets under the Basel III rule. The **Community Institution Mortgage Relief Act (H.R. 4521)** would have raised the CFPB's small servicer exemption threshold to give more community banks flexibility to use methods proved successful in holding down delinquency rates. This provision was also included in a number of other House bills **(H.R. 1750** and **H.R. 5786)**. Together, these bills would have preserved community bank servicing and deter further industry consolidation. Another bill, the **Access to Affordable Mortgages Act (H.R. 5148)**, would have allowed for in-house appraisals for higher priced mortgages of $250,000 or less provided they are held in portfolio. New appraisal standards have forced many community banks to hire appraisal management companies that frequently use appraisers from outside the area and produce lower quality appraisals than could be produced in-house. Portfolio lenders have every incentive to ensure appraisals are accurate. These additional mortgage provisions are discussed in more detail in the attached Plan for Prosperity. ICBA is hopeful many of these bills will be reintroduced in the 114th Congress.

ICBA also supports legislation that would exempt community banks from new information reporting requirements under the Home Mortgage Disclosure Act. Recent statutory requirements imposed the collection and reporting of 17 new HMDA data fields. Now, the CFPB is proposing financial institutions collect and report an additional 20 data fields beyond those included in the statute. The proposal will at least double the amount of information currently requested. Small community banks that manage the process manually will have to consider costly automation of the tasks associated with preparing the HMDA data file. Additionally, the type of data being proposed for collection is personal (i.e., age, credit score, debt-to-income, reasons for denial) and could make a customer more easily identifiable to the public. In sum, this new requirement represents a significant expense, puts customer privacy at risk, and is especially unwarranted when added to the already crushing burden of regulation.

Access to Capital

A second major theme of the Plan for Prosperity is capital access and preservation for community banks. A number of the provisions are dedicated to strengthening community bank viability by creating new options for capital raising and capital preservation.

One such provision, which was also included in S. 1349, would provide relief for community banks under $1 billion in asset size from the internal control attestation requirements of Section 404(b) of the Sarbanes-Oxley Act. Since community bank internal control systems are monitored continually by bank examiners, they should not have to incur the unnecessary annual expense of paying an outside audit firm for attestation work. This provision will substantially lower the regulatory burden and

expense for small, publicly traded community banks without creating more risk for investors.

Three capital provisions of the Plan for Prosperity would amend Basel III for banks with assets of $50 billion or less to restore the original intent of the accord which was intended to apply only to large, internationally active banks.

- *Exemption from the capital conservation buffer.* The new buffer provisions impose dividend restrictions that have a chilling effect on potential investors. This is particularly true for Subchapter S banks whose investors rely on dividends to pay their pro-rata share of the bank's tax. Exempting community banks from the capital conservation buffer would make it easier for them to raise capital.
- *Full capital recognition of allowance for credit losses.* Provide that the allowance for credit losses is included in tier 1 capital up to 1.25 percent of risk weighted assets with the remaining amount reported in tier 2 capital. This change would reverse the punitive treatment of the allowance under Basel III. The allowance should be captured in the regulatory capital framework since it is the first line of defense in protecting against unforeseen future credit losses.
- *Amend risk weighting to promote economic development.* Provide 100 percent risk weighting for acquisition, development, and construction loans. Under Basel III, these loans are classified as high volatility commercial real estate loans and risk weighted at 150 percent. ICBA's proposed change would treat these loans the same as other commercial real estate loans and would be consistent with Basel I.

ICBA also recommends reforming Regulation D so any person with a net worth of more than $1 million, including the value of their primary residence, would qualify as an "accredited investor." The number of non-accredited investors that could purchase stock under a private offering should be increased from 35 to 70. These Regulation D amendments have not previously been put into legislation.

These provisions were newly added to the Plan for Prosperity for the 114th Congress based on community banker feedback after reviewing and planning implementation of the new rule. None have yet been included in legislation.

Reforming Bank Oversight and Examination to Better Target Risk

A third major theme of the Plan for Prosperity is improving the exam environment for community banks. This includes three provisions as described below.

Call Reports

The quarterly call report filed by community banks now comprises 80 pages of forms and 670 pages of instructions. Implementation of the new Basel III capital standards may add nearly 60 additional pages to the already burgeoning call report. In September, nearly 15,000 community bankers representing 40 percent of all community banks nationwide

signed an ICBA petition to the regulatory agencies calling for more streamlined quarterly call report filings.

ICBA's recent Community Bank Call Report Burden Survey empirically demonstrates this problem. Eighty-six percent of survey respondents said the total cost of preparing the quarterly call report has increased over the last 10 years.[5] Thirty percent said it had increased significantly. A typical $500 million asset community bank, such as First National Bank of Scotia, spends close to 300 hours a year of senior level, highly-compensated staff time on the quarterly call report. By contrast, in 2001 my bank filed a 31 page call report. Our most recent call report was 80 pages. Though our bank has grown in asset size since 2001, no change in our basic business model justifies the addition of 50 pages to our call report. The growth of this burden has been dramatic.

Only a fraction of the information collected is actually useful to regulators in monitoring safety and soundness and conducting monetary policy. The 80 pages of forms contain extremely granular data such as the quarterly change in loan balances on owner-occupied commercial real estate. Whatever negligible value there is for the regulators in obtaining this type of detail is dwarfed by the expense and the staff hours dedicated to collecting it. To put things in perspective, consider this contrast: some large credit unions file a less-than-30 page call report. Surely, regulators can supervise community banks with significantly less paperwork burden than they currently demand.

For this reason, ICBA is calling on the agencies to allow highly-rated community banks to submit a short form call report in the first and third quarters of each year. A full call report would be filed at mid-year and at year-end. The short form would contain essential data required by regulators to conduct offsite monitoring, including income, loan growth, changes in loan loss reserves, and capital position. In the recent survey noted above, community bank respondents overwhelmingly agreed that instituting a short-form call report in certain quarters would provide a great deal of regulatory relief. Seventy-two percent of respondents indicated the relief would be substantial.

ICBA is seeking legislation that would require the banking agencies to institute call report reform as described above.

Extended Exam Cycle

Under current agency rules, a bank with assets of less than $500 million that has a CAMELS rating of 1 or 2 is eligible for an exam cycle of 18 months. Banks that do not meet these criteria are examined on a 12 month cycle. The extended exam cycle allows examiners to focus their limited resources on the banks that pose the greatest systemic risk. In order to more fully reap the benefit of risk-focused exams, the exam cycle can and should be further extended to 24 months and available to banks with assets up to $2 billion, provided they have a CAMELS rating of 1 or 2. Preparations for bank exams, and the exams themselves, distract bank management from serving their communities to their

---

[5] 2104 ICBA Community Bank Call Report Burden Survey.
http://www.icba.org/files/ICBASites/PDFs/2014CallReportSurveyResults.pdf

full potential. ICBA will pursue legislation in the 114th Congress to create an extended exam cycle as described above.

Strengthen Accountability in Examinations

The trend toward oppressive, micromanaged regulatory exams is an ongoing concern to community bankers nationwide. ICBA believes the best means of creating a more balanced exam environment is to create a workable appeals process. ICBA's Plan for Prosperity calls for the creation of an independent body to receive, investigate, and resolve material complaints from banks in a timely and confidential manner. The goal is to hold examiners accountable and to prevent retribution against banks that file complaints.

The current appeals process is arbitrary and frustrating. Appeals panels, or other processes, routinely lack the independence and market expertise necessary to reach a fair, unbiased decision.

The **Financial Institutions Examination Fairness and Reform Act (S. 727)**, introduced in the last Congress by Senators Moran and Manchin, would go a long way toward improving the oppressive examination environment by creating a workable appeals process and consistent, commonsense standards for classifying loans. This legislation would improve the appeals process by taking it out of the examining agencies and empowering a newly created Ombudsman, situated in the Federal Financial Institutions Examination Council, to make final appeals decisions. Though we favor additional measures to bring a higher level of accountability to the regulators and their field examiners, we are pleased to support the intent of this legislation. ICBA also thanks Senators Brown and Vitter for including this provision in the **Terminating Bailouts for Taxpayer Fairness Act of 2013 (S. 798).**

Additional Plan for Prosperity Provisions

Cost-Benefit Analysis of Proposed Rules

The financial regulatory agencies should be barred from issuing notices of proposed rulemaking unless they first determine that quantified costs are less than benefits. The analysis must take into account the impact on the smallest banks which are disproportionately burdened by regulation because they lack the scale and the resources to absorb the associated compliance costs. In addition, the agencies would be required to identify and assess available alternatives including modifications to existing regulations. They would also be required to ensure that proposed regulations are consistent with existing regulations, written in plain English, and easy to interpret.

ICBA is grateful to Chairman Shelby for introducing the **Financial Regulatory Responsibility Act of 2013 (S. 450)**, which closely mirrors the Plan for Prosperity provision. A similar bill **(H.R. 1060)** focused on SEC rulemakings passed the House in the 113th Congress. In addition, ICBA is pleased to support Section 9 of the **Startup Act**

(S. 181), recently introduced by Senators Moran and Warner, which would require prior agency review of proposed rules including a thorough assessment and quantification of the costs and benefits among other requirements. Each of these bills would offer welcome relief to community banks by putting a reasonable check on new regulations and ensuring that they do not jeopardize community banks' viability by imposing costs that outweigh any benefit.

Eliminate Burdensome Data Collection

The Plan for Prosperity calls for exempting banks with assets below $10 billion from the new small business data collection requirements. This requirement, which is in statute but has yet to be implemented by the CFPB, requires the reporting of information regarding every small business loan application. Think of it as HMDA for small business lending. Adding to the complexity, records of applications must be kept separate from records of the responses to applications and must be kept separate from the underwriting process. In other words, the requirement creates a separate bureaucracy within the bank that cannot be integrated with lending operations. This is especially inefficient, and may not be feasible in organizations that are too small to accommodate fire wall structures. Further, data collected by community banks and subsequently made public by the CFPB could compromise the privacy of applicants in small communities where an applicant's identity may be easily deduced, despite the suppression of personally identifying information.

ICBA is grateful to Senators Vitter and Brown for including in the **Too-Big-To-Fail Act (S. 798, 113th Congress)** a provision that would exempt banks with assets of $10 billion or less from the new small business data collection requirement. ICBA also supported the **Right to Lend Act (H.R. 2323)**, introduced in the 113th Congress by Rep. Pittenger, which would repeal the small business data collection requirement.

New Charter Option for Mutual Banks

Mutual community banks are among the safest and soundest financial institutions. They remained strong during the financial crisis and continued to provide financial services to their customers. The Plan for Prosperity calls for the creation of a new OCC charter for mutual national banks. This option would provide flexibility for institutions to choose the charter that best suits their needs and the communities they serve.

The Mutual Bank Choice and Continuity Act (H.R. 4252), introduced in the 113th Congress by Rep. Rothfus (R-PA) would have provided a national charter option for mutual banks, among other provisions.

Risk Targeting the Volcker Rule

The Plan for Prosperity calls for exempting banks with assets of $50 billion or less from the Volcker Rule. The Volcker Rule should apply only to the largest, most systemically risky banks. Approximately one year ago today we saw a vivid example of the unintended consequences of applying the Volcker Rule to community banks. The final

Volcker Rule, issued December 2013, required, in most instances, community banks to divest their holdings of collateralized debt obligations (CDO) TruPs by July 2015. This provision was unanticipated. Community banks would have been required to sell their investments at fire sale prices. Accounting standards require community banks to recognize immediately an impairment of their investments. Left unaddressed, this implementation of the Volcker Rule would have caused a significant and permanent loss of capital to hundreds of community banks. ICBA is grateful to this Committee for your support in persuading the agencies to reverse course on the Volcker Rule CDO Trups provision. This episode should convince all parties that banks with assets of $50 billion or less should be completely exempt from the Volcker Rule.

The Economic Growth and Regulatory Paperwork Reduction Act Review

While this statement has focused on legislative recommendations, I would also like to address the opportunity for agency regulatory relief presented by the 10-year review required under the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA).

The OCC, the Federal Reserve Board, and the FDIC are required to identify outdated, unnecessary or unduly burdensome regulation on insured depository institutions. This review will be conducted over a two-year period and will proceed by soliciting comment on twelve categories of regulation. This process holds real promise, if the agencies commit themselves to carrying it out in earnest and according to the terms of the statute.

Community bankers were significantly engaged in the last EGRPRA review, completed in 2006. More than 500 community bankers attended meetings around the country and many more submitted comment letters. Their input was substantive and detailed and should have formed the basis of significant regulatory relief. Unfortunately, the process was a lost opportunity and community bankers were deeply disappointed and disillusioned with the results. Though the process fully demonstrated the urgent need for relief, only minimal regulatory changes were made.

For this reason, ICBA is making specific recommendations with regard to the process to increase the chances the results match what was intended by Congress. These recommendations are detailed in our attached comment letter to the agencies. We urge this Committee to support our recommendations and to actively ensure the process results in significant regulatory relief. Community banks cannot afford another missed opportunity.

Closing

Thank you again for the opportunity to testify today. ICBA hopes this testimony, while not exhaustive, gives the Committee a sense of the sharply increasing resource demands

placed on community banks by regulation and examination and what's at stake for the future of community banking.

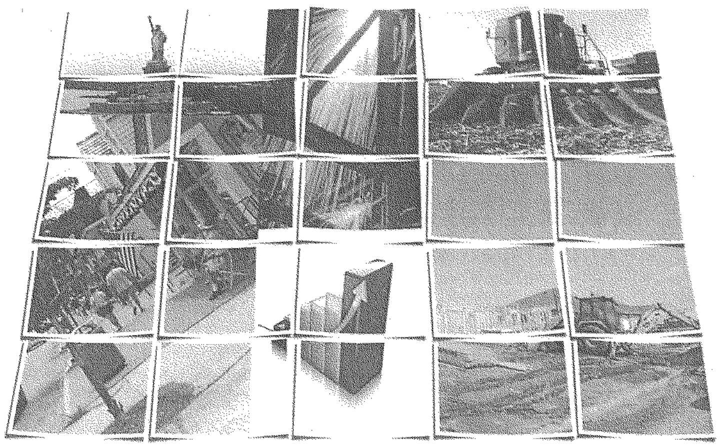
We urge that ICBA's Plan for Prosperity for the 114th Congress – as well as the CLEAR Relief Act and the other bills embodying Plan provisions introduced in the 113th Congress – serve as a guide to this committee. ICBA encourages you to reach out to the community bankers in your states. Ask them about the current regulatory environment and needed reforms. ICBA looks forward to working with this Committee to craft urgently needed legislative solutions.

ATTACHMENTS

- ICBA Plan for Prosperity. January 2015
- ICBA 2014 Community Bank Lending Survey Executive Summary and Infographic. January 2015
- List of Community Bank Regulatory Relief Bills from the 113Th Congress
- ICBA Comment Letter Regarding the Economic Growth and Regulatory Paperwork Reduction Act Process. September 2, 2014

INDEPENDENT COMMUNITY
BANKERS of AMERICA
One Mission. Community Banks.®

Plan for Prosperity



A Pro-Growth Agenda to Reduce the Onerous Regulatory Burden on Community Banks and Empower Local Communities
2015

Plan for Prosperity: An Agenda to Reduce the Onerous Regulatory Burden on Community Banks and Empower Local Communities

America's 6,500 community banks are vital to the prosperity of the U.S. economy, particularly in smaller towns and rural communities. Providing more than half of all small business loans under $1 million, as well as customized mortgage and consumer loans suited to the unique characteristics of their local communities, community banks serve a vital role in ensuring the economic recovery is robust and broad based, reaching communities of all sizes and in every region of the country.

In order to reach their full potential as catalysts for entrepreneurship, economic growth, and job creation, community banks must be able to attract capital in a highly competitive environment. An end to the exponential growth of onerous regulatory mandates is critical to this objective. Regulation is suffocating nearly every aspect of community banking and changing the very nature of the industry away from community investment and community building to paperwork, compliance, and examination. A fundamentally new approach is needed: Regulation must be calibrated to the size, lower-risk profile, and traditional business model of community banks.

ICBA's Plan for Prosperity provides targeted regulatory relief that will allow community banks to thrive by doing what they do best – serving and growing their communities. By reducing unsustainable regulatory burden, the Plan will ensure that scarce capital and labor resources are used productively, not sunk into unnecessary compliance costs, allowing community banks to better focus on lending and investing that will directly improve the quality of life in our communities. Each provision of the Plan was selected with input from community bankers nationwide and crafted to preserve and strengthen consumer protections and safety and soundness.

The Plan is a set of detailed legislative priorities positioned for advancement in Congress. A subset of these priorities is specifically dedicated to strengthening community bank viability by creating new options for capital raising and capital preservation. A number of regulatory relief measures would be tiered, with different thresholds for Consumer Financial Protection Bureau rules (generally $10 billion and under) and safety and soundness regulation (generally $50 billion and under). The recommended thresholds are based on existing levels and statutory provisions, which may vary by provision.

ICBA is committed to advancing and enacting the provisions of the Plan with all due vigilance and the aggressive use of every resource at our disposal. The Plan is a flexible, living document that can be adapted to a rapidly changing regulatory and legislative environment to maximize its influence and likelihood of enactment. Provisions are described below.

ACCESS TO CAPITAL: CREATING NEW OPTIONS FOR THE CREATION AND PRESERVATION OF COMMUNITY BANK CAPITAL

ICBA is proposing a set of options to strengthen community bank viability by enhancing access to capital.

Basel III Amendments: Restoring the Original Intent of the Rule. Basel III was originally intended to apply only to large, internationally active banks. ICBA proposes the following amendments for banks with assets of $50 billion or less.

- *Exemption from the capital conservation buffer.* The new buffer provisions impose dividend restrictions that have a chilling effect on potential investors. This is particularly true for Subchapter S banks whose investors rely on dividends to pay their pro-rata share of the bank's tax. Exempting community banks from the capital conservation buffer would make it easier for them to raise capital.
- *Full capital recognition of allowance for credit losses.* Provide that the allowance for credit losses is included in tier 1 capital up to 1.25 percent of risk weighted assets with the remaining amount reported in tier 2 capital. This change would reverse the punitive treatment of the allowance under Basel III. The allowance should be captured in the regulatory capital framework since it is the first line of defense in protecting against unforeseen future credit losses.
- *Amend risk weighting to promote economic development.* Provide 100 percent risk weighting for acquisition, development, and construction loans. Under Basel III, these loans are classified as high volatility commercial real estate loans and risk weighted at 150 percent. ICBA's proposed change would treat these loans the same as other commercial real estate loans and would be consistent with Basel I.

Additional Capital for Small Bank Holding Companies: Modernizing the Federal Reserve's Policy Statement. Require the Federal Reserve to revise the Small Bank Holding Company Policy Statement – a set of capital guidelines that have the force of law. The Policy Statement, which makes it easier for small bank and thrift holding companies to raise additional capital by issuing debt, would be revised to increase the qualifying asset threshold from $1 billion to $5 billion. Qualifying bank and thrift holding companies must not have significant outstanding debt or be engaged in nonbanking activities that involve significant leverage.

Relief from Securities and Exchange Commission Rules. ICBA recommends the following changes to SEC rules which would allow community banks to commit more resources to their communities without putting investors at risk:

- Provide an exemption from internal control attestation requirements for community banks with assets of less than $1 billion. The current exemption applies to any company with market capitalization of $75 million or less. Because community bank internal control systems are monitored continually by bank examiners, they should not have to sustain the unnecessary annual expense of paying an outside audit firm for attestation work. This provision will substantially lower the regulatory burden and expense for small, publicly traded community banks without creating more risk for investors.

- Due to an oversight in the 2012 JOBS Act, thrift holding companies do not have statutory authority to take advantage of the increased shareholder threshold below which a bank or bank holding company may deregister with the SEC. Congress should correct this oversight by allowing thrift holding companies to use the new 1,200 shareholder deregistration threshold as well as the new 2,000 shareholder registration threshold.
- Regulation D should be reformed so that anyone with a net worth of more than $1 million, including the value of their primary residence, would qualify as an "accredited investor." The number of non-accredited investors that could purchase stock under a private offering should be increased from 35 to 70.

TARGETED REGULATORY RELIEF

Supporting a Robust Housing Market: Mortgage Reform for Community Banks. Provide community banks relief from certain mortgage regulations, especially for loans held in portfolio. When a community bank holds a loan in portfolio, it has a direct stake in the loan's performance and every incentive to ensure it is properly underwritten, affordable and responsibly serviced. Relief would include:

- Providing "qualified mortgage" safe harbor status for loans originated and held in portfolio by banks with less than $10 billion in assets, including balloon mortgages.
- Exempting banks with assets below $10 billion from escrow requirements for loans held in portfolio.
- An exemption from the higher risk mortgage appraisal requirements for loans of $250,000 or less provided they are held in portfolio by the originator for a period of at least three years.
- New information reporting requirements under the Home Mortgage Disclosure Act should not apply to community banks.

Strengthening Accountability in Bank Exams: A Workable Appeals Process. The trend toward oppressive, micromanaged regulatory exams is a concern to community bankers nationwide. An independent body would be created to receive, investigate, and resolve material complaints from banks in a timely and confidential manner. The goal is to hold examiners accountable and to prevent retribution against banks that file complaints.

Reforming Bank Oversight and Examination to Better Target Risk. ICBA makes the following recommendations to allow bank examiners to better target their resources at true sources of systemic risk:

- A two-year exam cycle for well-rated community banks with up to $2 billion in assets would allow examiners to better target their limited resources toward banks that pose systemic risk. It would also provide needed relief to bank management for whom exams are a significant distraction from serving their customers and communities.
- Banks with assets of $50 billion or less should be exempt from stress test requirements.
- Community banks should be allowed to file a short form call report in the first and third quarters of each year. The current, long form call report would be filed in the second and fourth quarters. The quarterly call report now comprises some 80 pages supported by almost 700 pages of instructions. It represents a growing burden on community banks without being an effective supervisory tool.

Redundant Privacy Notices: Eliminate Annual Requirement. Eliminate the requirement that financial institutions mail annual privacy notices even when no change in policy has occurred. Financial institutions would still be required to notify their customers by mail when they change their privacy policies, but when no change in policy has occurred, the annual notice provides no useful information to customers and is a needless expense.

Balanced Consumer Regulation: More Inclusive and Accountable CFPB Governance. The following changes would strength CFPB accountability, improve the quality of the agency's rulemaking, and make more effective use of its examination resources:

- Change the governance structure of the CFPB to a five-member commission rather than a single Director. Commissioners would be confirmed by the Senate to staggered five-year terms with no more than three commissioners affiliated with any one political party. This change will strengthen accountability and bring a diversity of views and professional backgrounds to decision-making at the CFPB.
- The Financial Stability Oversight Council's review of CFPB rules should be strengthened by changing the vote required to veto a rule from an unreasonably high two-thirds vote to a simple majority, excluding the CFPB Director.
- All banks with assets of $50 billion or less should be exempt from examination and enforcement by the CFPB; and CFPB backup (or "ride along") authority for compliance exams performed by a bank's primary regulator should be eliminated.

Eliminate Arbitrary "Disparate Impact" Fair Lending Suits. Amend the Equal Credit Opportunity Act and the Fair Housing Act to bar "disparate impact" causes of action. Lenders that uniformly apply neutral lending standards should not be subject to frivolous and abusive lawsuits based on statistical data alone. Disparate impact forces lenders to consider factors such as race and national origin in individual credit decisions, which are specifically precluded by law.

Ensuring the Viability of Mutual Banks: New Charter Option. The OCC should be allowed to charter mutual national banks to provide flexibility for institutions to choose the charter that best suits their needs and the communities they serve.

Rigorous and Quantitative Justification of New Rules: Cost-Benefit Analysis. Provide that financial regulatory agencies cannot issue notices of proposed rulemakings unless they first determine that quantified costs are less than benefits. The analysis must take into account the impact on the smallest banks which are disproportionately burdened by regulation because they lack the scale and the resources to absorb the associated compliance costs. In addition, the agencies would be required to identify and assess available alternatives including modifications to existing regulations. They would also be required to ensure that proposed regulations are consistent with existing regulations, written in plain English, and easy to interpret.

Cutting the Red Tape in Small Business Lending: Eliminate Burdensome Data Collection. Exclude banks with assets below $10 billion from new small business data collection requirements. This provision, which requires the reporting of information regarding every small business loan application, falls disproportionately upon community banks that lack scale and compliance resources.

Preserve Community Bank Mortgage Servicing. The provisions described below would help preserve the important role of community banks in servicing mortgages and deter further industry consolidation, which is harmful to borrowers:

- Increase the "small servicer" exemption threshold to 20,000 loans (up from 5,000). To put this proposed threshold in perspective, the average number of loans serviced by the five largest servicers subject to the national mortgage settlement is 6.8 million. An exemption threshold of 20,000 would demarcate small servicers from both large and mid-sized servicers.
- For banks with assets of $50 billion or less, reverse the punitive Basel III capital treatment of mortgage servicing rights (MSRs) and allow 100 percent of MSRs to be included as common equity tier 1 capital.

Creating a Voice for Community Banks: Treasury Assistant Secretary for Community Banks. Economic and banking policies have too often been made without the benefit of community bank input. An approach that takes into account the diversity and breadth of the financial services sector would significantly improve policy making. Creating an Assistant Secretary for Community Banks within the U.S. Treasury Department would ensure that the more than 6,500 community banks across the country, including minority banks that lend in underserved markets, are given appropriate and balanced consideration in the policy making process.

Modernize Subchapter S Constraints. Subchapter S of the tax code should be updated to facilitate capital formation for community banks, particularly in light of higher capital requirements under the proposed Basel III capital standards. The limit on Subchapter S shareholders should be increased from 100 to 200; Subchapter S corporations should be allowed to issue preferred shares; and Subchapter S shares, both common and preferred, should be permitted to be held in individual retirement accounts (IRAs). These changes would better allow the nation's 2,200 Subchapter S banks to raise capital and increase the flow of credit.

Five-Year Loss Carryback Supports Lending During Economic Downturns. Banks with $15 billion or less in assets should be allowed to use a five-year net operating loss (NOL) carryback. The five-year NOL carryback is countercyclical and will support community bank capital and lending during economic downturns.

Risk Targeting the Volcker Rule. Exempt banks with assets of $50 billion or less from the Volcker Rule. The Volcker Rule should apply only to the largest, most systemically risky banks. Proposals to apply the rule to community banks carry unintended consequences that threaten to destabilize segments of the community banking industry.

The Independent Community Bankers of America®, the nation's voice for 6,500 community banks of all sizes and charter types, is dedicated exclusively to representing the interests of the community banking industry and its membership through effective advocacy, best-in-class education and high-quality products and services. For more information, visit www.icba.org.

2014 ICBA Community Bank Lending Survey

Executive Summary

January 2015

ICBA
INDEPENDENT COMMUNITY BANKERS of AMERICA®
www.icba.org

ICBA
INDEPENDENT COMMUNITY
BANKERS of AMERICA®

2014 ICBA Community Bank Lending Survey – Executive Summary

In 2014, ICBA conducted a survey of community banks on their lending activities. The survey provides a valuable benchmark to help gauge community banks' outlook toward areas of lending in the year ahead, real-world data to help policymakers assess the impact of recent rulemaking and insights into barriers that are preventing community banks from better serving their communities.

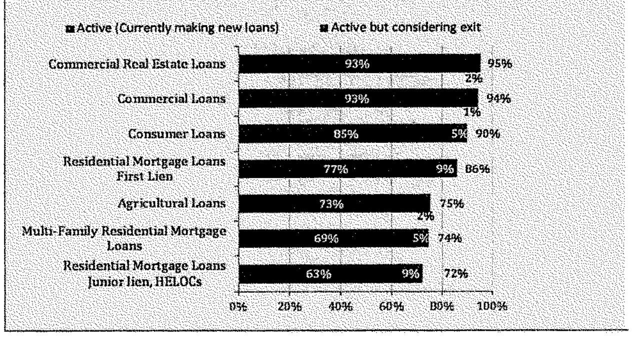
Key Findings:

- Most community banks are full-service lenders, providing many different types of loans to meet their customers' needs.
- Despite challenges, community banks maintain a positive outlook towards most areas of lending.
- The regulatory burden is putting pressure on community banks' residential mortgage lending activities.
- Exemptions from the Consumer Financial Protection Bureau Qualified Mortgage (QM) rule for small and rural creditors are too narrow and risk limiting consumer access to mortgage credit.
- Community banks perceive making non-QM mortgages as a significant risk and are reluctant to do so.
- Community banks' loan underwriting trended towards tighter standards across all lines of lending.

Analysis:

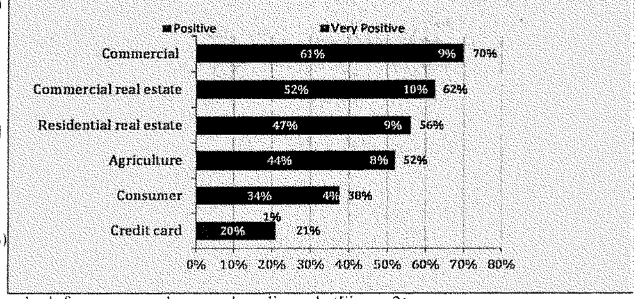
Most community banks are full-service lenders, providing many different types of loans to meet their customers' needs. Almost all banks are active in the area of commercial real estate (95%), commercial, (94%) and consumer lending (90%, Figure 1).

Figure 1: Community Bank Lending Activity in 2013-14 – Active Lending Areas



ICBA
INDEPENDENT COMMUNITY
BANKERS of AMERICA®

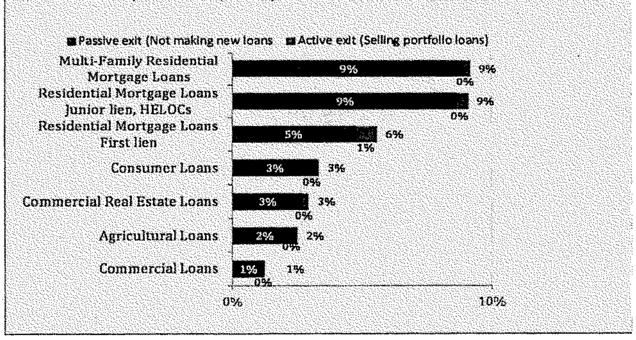
Figure 2: Community Bank Lending Outlook by Area – Positive



Despite many challenges, community banks maintain a positive outlook towards most areas of lending over the next two years. The most positive outlook was for commercial lending (70%) and commercial real estate lending (62%). Fewer respondents, though still a majority, had a positive outlook for residential real estate (56%) and agriculture (52%) loans. Only a minority of respondents had a positive outlook for consumer loans and credit cards (Figure 2).

Regulatory burden is putting pressure on community banks' residential mortgage lending activities. The regulatory burden of new rules and requirements was the most cited (73%) barrier to making more residential mortgage loans (Figure 5). (Relatively few banks cited this factor for consumer (26%) or commercial (21%) lending.) Additionally, while most banks (86%, Figure 1) remain active residential mortgage lenders, a significant percentage are considering an exit (9%), are exiting from this line of lending (6%, Figure 3) or are not active (9%, Figure 4). A majority of banks reported tighter underwriting in residential mortgage lending (57%) and many reported decreases in originations (44%). Most community banks reported having increased staffing for lending compliance in the last five years (78%).

Figure 3: Community Bank Lending Activity in 2013-14 – Exit Lending Areas



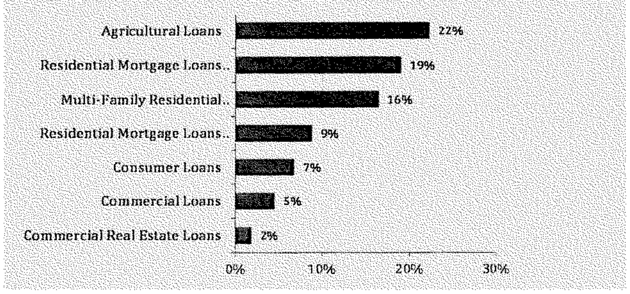
Exemptions from the Consumer Financial Protection Bureau Qualified Mortgage (QM) rule for small and rural creditors are too narrow. Though they meet the asset threshold test of $2 billion or less, two-thirds of banks with $500 million to $2 billion in assets make too many loans (more than 500 a year) to qualify (66%). Half of banks that serve rural areas do not qualify for the "rural" exception (50%).

Community banks perceive making non-QM mortgages as a significant

ICBA
INDEPENDENT COMMUNITY
BANKERS of AMERICA®

risk and are reluctant to do so. Only one-quarter of community banks routinely make non-QM loans (25%). Two-thirds of community banks simply do not make non-QM mortgage loans (44%) or only do so in special cases (22%).

Figure 4: Community Bank Lending Activity in 2013-14 – Inactive Lending Areas

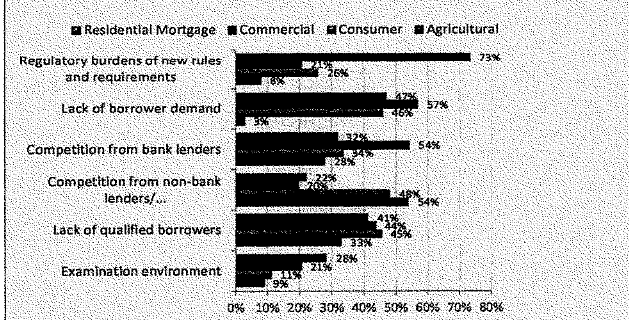


While most community banks reported underwriting standards remained unchanged in 2013-14 compared to the previous two-year period, many more banks reported tighter underwriting standards than looser. About one-in-three banks reported tighter underwriting standards in commercial real estate (38%), commercial loans (32%), agricultural loans (32%) and consumer loans (30%). Less than 1 in 20 reported looser underwriting for any type of lending.

The majority of banks reported increased loan originations in 2014 compared to the previous year for commercial loans (52%), commercial real estate (52%) and agricultural loans (51%). In contrast, a significant number of community banks experienced decreases in consumer loan originations (27%).

Market factors prevented community banks from making more commercial and consumer loans. Lack of borrower demand was cited by a majority of respondents for commercial loans (57%). Just under half of respondents cited this factor for mortgage (47%) and consumer lending (46%). Lack of qualified borrowers was cited by more than four-in-ten banks for consumer (45%), commercial (44%) and mortgage lending

Figure 5: Factors Preventing Community Banks from Making More Loans



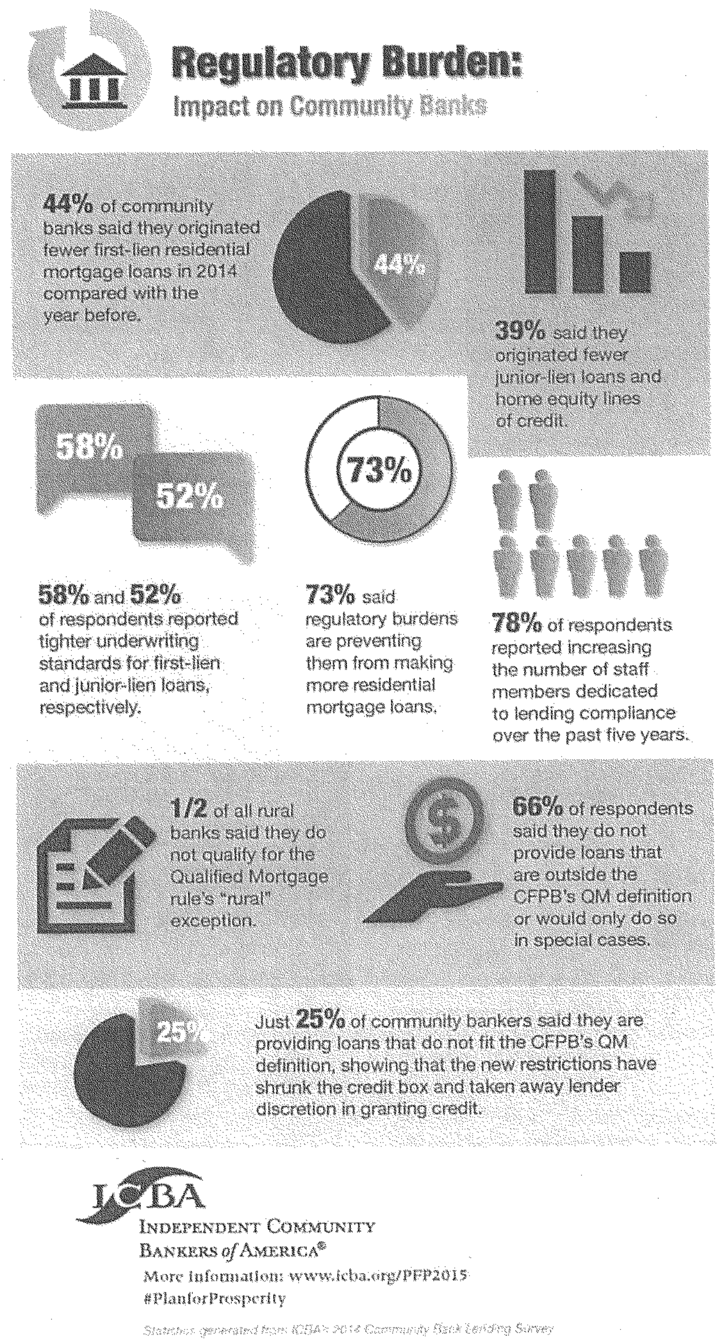
(41%, Figure 5).

Competition from other banks, non-banks and government agencies is also an important limiting factor in community bank lending. Competition from non-bank lenders was the top factor preventing banks from making more consumer loans (48%) and competition from bank lenders was the second most cited factor in commercial loans (54%). Agricultural lenders cited competition from the Farm Credit System as the top factor (54%, Figure 5).

Survey Methodology:
The ICBA Community Bank Lending Survey was distributed by email to 6,500 community banks. Between September 15 and October 3, 2014, 519 unique responses were collected on a one response per bank basis, for a response rate of 8.0%. Most responses (79%) came from either the bank president and CEO (59%) or the chief lending officer (20%).

The survey sample slightly over-represents community banks between $50 million and $500 million in assets and under-represents community banks above $500 million in assets compared to the industry below $10 billion in assets. In terms of regulator, charter and ownership type, survey respondents closely reflect the make-up of the industry below $10 billion in assets. When asked to indicate the types of geographic areas they served (multiple selections were allowed), 20% of respondents indicated urban areas, 39% suburban areas and 76% serve rural areas.

Infographic: ICBA 2014 Community Bank Lending Survey



Community Bank Regulatory Relief Bills in the 113th Congress

Bills Enacted in the 113th Congress

Title, Bill #, Date of Passage	Sponsor(s)	Description
H.R. 3329, 5/6/14	Luetkemeyer	Requires the Federal Reserve to revise the Small Bank Holding Company Policy Statement by increasing the qualifying asset threshold from $500 million to $1 billion

Bills Passed the Senate

Community Bank Preservation Act (S. 2252) *Passed as an amendment to S. 2244. Subsequently enacted in the 114th Congress.*	Vitter	Requires that at least one member of the Board of Governors of the Federal Reserve has experience as a community banker or as a supervisor of community banks.

Senate Bills Introduced

Consumer Financial Protection Bureau Examination and Reporting Threshold Act of 2014, S. 2732	Toomey, Donnelly	Raises the exemption threshold for CFPB examinations from $10 billion to $50 billion
HELP Rural Communities Act, S. 1916	McConnell	Creates a petition process with regard to the CFPB's designation of an area as "rural"
CLEAR Relief Act of 2013, S. 1349	Moran, Tester, Kirk	Portfolio QM for banks under $10 billion, escrow exemption for portfolio loans held by banks under $10 billion, SARBOX 404(b) exemption for banks under $1 billion, raise SBHC threshold to $5 billion
Terminating Bailouts for Taxpayer Fairness Act of 2013, S. 798	Brown, Vitter	Broadens "rural" definition, bank exam reform (provisions of S. 727), privacy notice relief, shareholder threshold fix for thrift holding companies, mutual holding company dividend relief, raise SBHC threshold to $5 billion, exemption from small business data collection for banks under $10 billion
Financial Institutions Examination Fairness and Reform Act, S. 727	Moran, Manchin	Create an Ombudsman within the Federal Financial Institutions Examination Council to hear appeals of exam findings
Privacy Notice Modernization Act, S. 635	Brown, Moran	Privacy notice relief
Municipal Advisor Relief Act, S. 710	Toomey, Warner	Exempt banks and bank employees from registration

Responsible Financial Consumer Protection Regulations Act, S. 205	Moran	Replaces the single CFPB Director with a Senate-confirmed, five-person Commission, among other provisions
Holding Company Registration Threshold Equalization Act, S. 872	Toomey, Pryor	Allows thrift holding companies to use the new shareholder registration and deregistration thresholds
The Financial Regulatory Responsibility Act of 2013, S. 450	Shelby	Prohibits any federal financial regulatory agency from publishing a notice of final rulemaking if it determines that the quantified costs are greater than the quantified benefits
S. 2641	Landrieu	Provides QM status to any mortgage held in portfolio by a bank of less than $10 billion

Bills Passed by the House

Title, Bill #, Date of Passage	Sponsor(s)	Description
Eliminate Privacy Notice Confusion Act, H.R. 749, 3/12/13	Luetkemeyer	Eliminate the requirement that financial institutions mail annual privacy notices when no change in policy has occurred
SEC Regulatory Accountability Act, H.R. 1062, 5/17/13	Garrett	Requires the Chief Economist of the SEC to determine that the benefits of any proposed regulation justify the costs before adopting such regulation
Holding Company Registration Threshold Equalization Act H.R. 801, 1/14/14	Womack, Himes	Allows thrift holding companies to use the new shareholder registration and deregistration thresholds
Consumer Financial Protection Commission Act, H.R. 3193, 2/27/14	Duffy	Replaces the single CFPB Director with a five-person Commission, strengthens FSOC review of CFPB rules, among other provisions
Helping Expand Lending Practices in Rural Communities Act, H.R. 2672, May 6, 2014	Barr	Creates a petition process with regard to the CFPB's designation of an area as "rural"

Passed by the Financial Services Committee but not House

Path Act, H.R. 2767, 7/24/13	Garrett, Hensarling	Portfolio QM, escrow relief, raise servicing exemption threshold, exam relief, QRM repeal
Portfolio Lending and Mortgage Access Act of 2013, H.R. 2673, 5/7/14	Barr	Portfolio QM
Community Institution Mortgage Relief Act, H.R. 4521, 5/7/14	Luetkemeyer	Escrow relief for portfolio loans for banks under $10 billion, raise small servicer exemption to 20,000 loans

Financial Regulatory Clarity Act, H.R. 4466	Capito, Meeks	Requires financial regulators, before issuing any new rule, to consider whether it is in conflict, is inconsistent with, or is duplicative of an existing rule
Access to Affordable Mortgages Act, H.R. 5148	Luetkemeyer	Creates an exemption from the higher risk mortgage appraisal requirement for loans of $250,000 or less provided they are held in portfolio.
Community Bank Mortgage Servicing Asset Capital Requirements Study Act, H.R. 4042	Luetkemeyer	Delays the effective date of the Basel III rule with respect to MSAs for nonsystemic banking institutions and requires the banking agencies to conduct a joint study of the appropriate capital treatment of MSAs.

House bills introduced but not considered in Committee

CLEAR Relief Act, H.R. 1750	Luetkemeyer	Portfolio QM, escrow relief, raise servicing exemption threshold, appraisal relief, privacy notices, SARBOX 404(b) exemption, SEC cost-benefit, SBHC threshold
JOBS Act, H.R. 4304	Scalise	All provisions of H.R. 1750, the CLEAR Act
Financial Institutions Examination Fairness and Reform Act , H.R. 1553	Capito, Maloney	Create an Ombudsman within the Federal Financial Institutions Examination Council to hear appeals of exam findings
Municipal Advisor Oversight Improvement Act, H.R. 797	Stivers	Exempts enumerated traditional banking activities from triggering the registration requirement
Mutual Community Bank Competitive Equality Act, H.R. 1603	Grimm, Meeks, King	Allows the OCC to charter mutual national banks. Permits a mutual holding company to waive dividends paid by its stock subsidiary if specified conditions are met
Mutual Bank Choice and Continuity Act, H.R. 4252	Rothfus	Provides a national charter option for mutual banks and allow mutual banks to issue Mutual Capital Certificates (MCCs) that would qualify as Tier 1 common equity capital
Right to Lend Act, H.R. 2323	Pittenger	Repeals Section 1071 of the Dodd-Frank Act, which requires HMDA-like data collection for commercial lending
Small Financial Institutions Regulatory Relief Act H.R. 5786	Lankford, Welch	QM status and escrow relief for portfolio mortgages held by lenders under $10 billion; raise small servicer threshold to 10,000 loans; privacy notices, Small Bank Holding Company; Fed governor; create application process for rural designation
S Corporation Modernization Act, H.R. 892	**Reichert, Kind**	**Allows S corporation shares to be held in an individual retirement account**

ICBA
INDEPENDENT COMMUNITY
BANKERS of AMERICA®

September 2, 2014

Robert deV. Frierson, Secretary
Board of Governors
Federal Reserve System
20th Street and Constitution
Washington, DC 20551

Robert E. Feldman, Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

Legislative and Regulatory Activities Division
Office of the Comptroller of the Currency
400 7th Street SW
Washington, DC 20219

Re: Regulatory Publication and Review Under the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA), Docket No. FFIEC-2014-0001; Fed Docket No. OP-1491;

Dear Sirs or Madam:

The OCC, the Federal Reserve Board, and the FDIC are conducting a review of the regulations they have issued to identify outdated, unnecessary or unduly burdensome regulation on insured depository institutions. This review is required under the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (EGRPRA) and will be conducted over a two year period. The Independent Community Bankers of America (ICBA)[1] appreciates the opportunity to comment on the first notice that was published by the banking agencies under EGRPRA to help identify those regulations in the first three categories of regulations that are outdated, unnecessary or unduly burdensome.

1 *The Independent Community Bankers of America®, (ICBA), the nation's voice for more than 6,500 community banks of all sizes and charter types, is dedicated exclusively to representing the interests of the community banking industry and its membership through effective advocacy, best-in-class education and high-quality products and services.*

ICBA members operate 24,000 locations nationwide, employ 300,000 Americans and hold $1.3 trillion in assets, $1 trillion in deposits and $800 billion in loans to consumers, small businesses and the agricultural community. For more information, visit www.icba.org.

Under EGRPRA, the banking agencies will review more than a hundred subject areas of regulations. The banking agencies have grouped these regulations into twelve regulatory categories. Over the next two years, the agencies plan to publish four Federal Register notices, each addressing one or more categories of rules. Our understanding is that the CFPB will not be a part of this process, but is required to review its significant rules and publish a report of its review no later than five years after they take effect.

This letter will comment not only on the first three categories of regulations—Applications and Reporting, Powers and Activities, and International Operations—but will also comment generally on the EGRPRA process and also the severe regulatory environment that community banks now face.

EGRPRA Process

ICBA and its members were very actively engaged during the first EGRPRA review process which was conducted from 2004 to 2006. ICBA members and staff attended many of the outreach meetings and extensively commented on all six of the published EGRPRA notices. According to the final EGRPRA report that the FFIEC published in the Federal Register and sent to Congress in 2007[2], there were sixteen EGRPRA outreach sessions around the country involving more than five hundred participants, most of whom were community bankers. At the St. Louis outreach session, for instance, there were almost one hundred community banks represented. The agencies received 850 letters from bankers, consumer and community groups, trade associations, and other interested parties in response to their comment requests.

Despite the strong involvement and input from community banks during the first EGRPRA review process, community banks and the ICBA were deeply disappointed and disillusioned with the outcome. Since few substantive regulations were repealed, eliminated or substantially amended by the banking agencies, many community bankers have concluded that EGRPRA is no more than a "check the box" regulatory process. On the major issues raised by the bankers in 2004 to 2006, such as repealing the right of rescission under the Truth in Lending Act, raising the $10,000 Currency Transaction Report threshold, or reducing disclosures under the Home Mortgage Disclosure Act, the banking agencies either rejected the recommendations outright or deferred action until further study could be completed.

Overall, the banking agencies believed that their first EGRPRA review had been a success because they were able to eliminate some duplicative regulation, or accomplish such things as redesigning their financial institution letters, or streamlining their branch application procedures. However, these changes hardly made an impact on the overall regulatory burden that now confronts community banking.

If the new EGRPRA process is to have any chance at success, there must be a strong commitment by the heads of the banking agencies to do what is necessary to eliminate regulation that is outdated, unnecessary or unduly burdensome. The

[2] See the Federal Register, Volume 72, No. 211 on November 1, 2007.

EGRPRA statutory mandate requires the agencies to go beyond merely streamlining regulations, tweaking certain regulations, eliminating duplication, or deferring action until some further interagency study can be completed. Rather, the mandate requires the agencies to thoroughly review each regulation and eliminate it if it is outdated, unnecessary or unduly burdensome.

This will require the agencies to consider the costs and benefits of each regulation and to carefully consider the input they receive from community bankers. Furthermore, even if there are some benefits to having a regulation, it should be eliminated under the EGRPRA process if it can be shown to be unduly burdensome.

Furthermore, ICBA urges the banking agencies to hold at least six outreach meetings around the country to gather the input and testimony of community banks. At these outreach meetings, community bankers should be allowed to discuss the overall regulatory burden and how it could be reduced. For those bankers that are unable to attend the outreach meetings, they should be permitted to participate remotely by phone. The best way to truly assess the costs and benefits of banking regulation is to hear the personal experiences and testimony of bankers.

The banking agencies also should set up an EGRPRA.gov website as they did during the first review. On the website, the agencies can post the comment letters they receive, post the notices that are published in the Federal Register, and list the regulations that bankers mention the most as being outdated, unnecessary or unduly burdensome. There could be a top ten list of the most burdensome regulations which would include those regulations that are mentioned the most at the outreach meetings and in banker comment letters. The EGRPRA.gov website could also post notices about the outreach meetings and summaries of each meeting.

Finally, there should be an overall director of the current EGRPRA interagency review process—an EGRPRA czar—who has a strong commitment to reducing unnecessary and unduly burdensome regulation and who can, in certain situations, overcome the objections of individual agencies to specific recommendations and resolve interagency disputes. Too often during the last EGRPRA review process, burden reducing recommendations were rejected because of the objection of one agency or because the agencies could not achieve a consensus. This director or EGRPRA czar should have the authority to overrule such objections where it is clear that the regulation is unduly burdensome. There will always be someone who can find some reason to preserve a regulation so, to ensure an effective process, there should be a director who can overcome such objections.

The Overall Regulatory Burden on Community Banks

In the preface to the last EGRPRA report in 2007, John Reich, who at that time was not only the Director of the Office of Thrift Supervision but also the leader of the interagency EGRPRA program, warned of the consequences to community banking if the regulatory burden was not reduced. He said:

> "Financial institutions of all sizes suffer under the weight of unnecessary regulatory burden, but small community banks unquestionably bear a disproportionate share of the burden due to their more limited resources. While it is difficult to accurately measure the impact regulatory burden has played in industry consolidation, numerous anecdotal comments from bankers across the country as well as from investment bankers who arrange merger and acquisition transactions indicate it has become a significant factor. Accordingly, I am deeply concerned about the future of our local communities and the approximately 8,000 community banks under $1 billion in assets..."

Since John Reich's statement in 2007, the number of community banks has dropped to about 6,500 due mainly to consolidation, and the amount of regulation has grown exponentially.

Several recent studies have attempted to quantify the overwhelming regulatory burden on community banking. For instance, according to a recent KPMG Banking Industry Outlook Survey[3], sixty percent of bankers said that regulatory requirements account for as much as 10 percent of their total operating costs and that 22 percent said that complying with the regulation is responsible for as much as 11 to 20 percent of their total operating costs. As KPMG concludes, "This significantly adds to the pressure that banks are already feeling to keep costs down to deliver the returns investors expect while also raising the higher levels of capital now required."

The Mercatus Center at George Mason University recently produced a high quality empirical study[4] on the impact of regulations on community banks since the Dodd-Frank Act was enacted in 2010. The study, which is based on a survey of approximately 200 community banks in 41 states with less than $10 billion in assets, is largely consistent with the anecdotal evidence. Broad findings from the study include:

- **Additional costs.** Approximately 90 percent of respondents reported that compliance costs have increased since 2010. 83 percent reported that they had increased by more than 5 percent.
- **Outside consultants.** More than half of surveyed community banks (51%) anticipate engaging with outside consultants in connection with the Dodd-Frank Act requirements, and an additional 21 percent are unsure.
- **Additional compliance personnel.** Since 2010, the respondent banks said they have hired additional compliance/legal personnel. 27 percent of respondents plan to hire additional compliance/legal personnel in the next 12 months, and an additional 28 percent are unsure. The survey also finds that employees not exclusively dedicated to compliance, including CEOs and senior managers, are forced to spend more time on compliance issues.

---

[3] The KPMG study can be found at:
http://www.kpmginfo.com/industryoutlooksurveys/2014/pdfs/KPMGBankingIndustrySurvey_072414.pdf

[4] "How are Small Banks Faring Under Dodd-Frank?" Hester Peirce, Ian Robinson, and Thomas Stratmann. Mercatus Center Working Paper. February 2014.

1615 L Street NW, Suite 900, Washington, DC 20036-5623 | 800-422-8439 | FAX: 202-659-1413 | Email: info@icba.org | Website: www.icba.org

- **Regulation is driving consolidation.** 26 percent of respondents anticipate that their bank will engage in merger activity in the next five years, and another 27 percent are unsure. 94 percent of banks anticipate further industry consolidation.

The anecdotal evidence is also compelling. ICBA established an EGRPRA website so that its members could give some feedback online about EGRPRA and regulatory burden. One banker expressed the frustrations of many community banks with this comment:

> "Banking has become the most highly regulated industry in the world. Legislation and regulation created to address problems caused by the largest banks has been foisted upon all banks. As such, we are seeing the life-blood sucked out of our local communities. Meanwhile, un-taxed credit unions, already held to a much lower standard of compliance, are allowed seemingly unbridled growth. They now boast membership exceeding 100 million... When coupled with the Farm Credit System loaning any amount to anyone at any rate they choose, you have a serious problem for the continued viability of community banking in this country. Meanwhile, "back at the ranch", you have community bankers, many of whose institutions have been in business for 100+years, seriously considering folding up their tent. I would add that the creation of the Consumer Financial Protection Bureau, with its annual payroll now exceeding $200 million, will do nothing but increase costs to consumers and make the problems worse. We need less regulation, not more; less government, not more; more action and less talk.

The Mercatus Study noted above also reported narrative comments from respondents about regulation. Here are a few examples:

- "We don't have the number of employees or the financial resources to keep up with [new] rules ... Why make it harder for community banks to do business and survive? We fill a niche that larger banks can't and won't."
- "Community banks that know their customers will struggle to be able to continue to lend to good, long-term customers."
- "Many concerned, conscientious community bankers are selling out or just retiring due to the maddening pace of illogical and unnecessary regulation. Not one of the regulations we've seen would have done anything to prevent the 2008 collapse."

These comments, offered anonymously by bankers, illustrate how increasing regulatory burden is fundamentally changing the nature of the business of community banking.

Community banks play a crucial role in the economic life of rural areas and small communities passed over by larger banks. The credit and other financial services they provide in these communities will help advance and sustain the economic recovery and ensure that it reaches every corner of the country. Community banks are responsible for 60 percent of all small business loans under $1 million. As the economic recovery

1615 L Street NW, Suite 900, Washington, DC 20036-5623 | 800-422-8439 | FAX: 202-659-1413 | Email: info@icba.org | Website: www.icba.org

strengthens, small businesses will lead the way in job creation with the help of community bank credit.

The role of community banks in advancing and sustaining the recovery is jeopardized by the increasing expense and distraction of regulation drastically out of proportion to any risk they pose. **Community banks didn't cause the recent financial crisis, and they should not bear the weight of new, overreaching regulation intended to address it.**

ICBA urges the regulatory agencies as part of the EGRPRA process to conduct their own empirical study of the regulatory burden on community banks to quantify the burden and confirm what the KPMG, Mercatus and other studies are showing—that the burden is significant and is driving community banks out of the business of banking. Such a study could also identify those regulations that are the most burdensome. The FDIC attempted to conduct such a study as part of its 2012 Community Bank Study. In the appendix to that study, the FDIC summarized its interviews with community bankers concerning regulatory compliance costs but failed to quantify the costs, after concluding it would be difficult.

We urge the FDIC, the OCC, and the Federal Reserve to confirm what community bankers are also saying anecdotally—that each new regulation is not only reducing the franchise value of their banks but also impairing the ability of their banks to lend to the communities they serve.

Specific Comments on the Three Categories of Regulations

ICBA has a number of specific burden reducing recommendations regarding the first two of the three categories of regulation that the agencies have requested comments on—Applications and Reporting and Powers and Activities. We have no comments on International Operations regulations.

Call Report Burden. With 80 pages of forms to complete and over 670 pages of instructions, the call report has become a significant regulatory burden for community banks to prepare. In fact, as new regulations are issued and old ones are amended, the call report just gets more complicated and more burdensome to prepare. From that perspective, the call report really has become a symbol of the overall regulatory burden community banks currently experience.

For instance, the call report has grown from 18 pages in 1986 to 29 pages in 2003 to nearly 80 pages today! Just recently the regulators proposed another 57 pages of instructions because of the new Basel III regulatory capital framework. The call report—which community banks submit every 65 business days—has more pages than the typical U.S. community bank has employees. Community banks have very limited resources available to tackle the challenges faced when trying to meet ever changing regulatory reporting requirements that do not properly consider the size and complexity of the institution.

1615 L Street NW, Suite 900, Washington, DC 20036-5623 | 800-422-8439 | FAX: 202-659-1413 | Email: info@icba.org | Website: www.icba.org

ICBA's recently released its 2014 Community Bank Call Report Burden Survey.[5] According to the survey, 86 percent of community bank respondents said that the annual cost of preparing the report has increased over the past ten years. Further, 98 percent of respondents said ICBA's proposed short-form call report, which qualifying community banks would be able to submit for the first and third quarters of each year, would reduce their regulatory burden. Seventy-two percent said the burden reduction would be substantial. The survey also showed that over the last ten years the number of hours required to complete the call report and the resources involved with meeting reporting obligations has increased.

Recent expansions of the use of the call report as an information gathering tool for consumer protection regulation further damage the effectiveness of the information provided and the use of the report as a safety and soundness metric. ICBA notes that regulated credit unions are not required to produce anywhere near the level of detail that is required by community banks even though their depositors are offered the same levels of protection and they engage in similar and in some cases identical activities as community banks. For example, in the first quarter of 2014, the smallest community bank was required to submit a call report that is 80 pages in length while the largest credit union in the country with over $58 billion in assets submitted a call report with only 28 pages.

ICBA believes that highly rated, well-capitalized community banks would benefit greatly from a call reporting structure that allows them to file a short-form call report covering the first and third quarters and a long-form call report for the second and fourth quarters of each year. Preparers of community bank call reports believe that preparing a short-form call report with limited schedules in certain quarters would reduce the overall time required to meet call reporting obligations and reduce regulatory burden substantially. Without immediate relief for community banks that reduces the current regulatory burden including the increasingly taxing call report requirements, consolidation of community banks in the United States will occur at a rapid rate.

ICBA strongly urges the banking agencies to work actively together to amend the current call report burden by allowing community banks to make use of the short-form call report solution. With only approximately 60 business days between reporting periods, instituting the short-form call report solution will greatly alleviate limited community bank resources that would be better deployed meeting the needs of local communities without compromising on the valuable metrics needed to efficiently assess safety and soundness. ICBA is proposing that in the community bank's fiscal first and third quarters, the complete call report would be replaced by a short-form call report that includes only limited financial schedules such as the income statement, balance sheet, and statement of changes in bank equity capital. These schedules would provide the agencies with sufficient information to detect any significant changes in condition that might warrant additional follow up.

[5] ICBA's 2014 Community Bank Call Report Burden Survey can be found at http://www.icba.org/files/ICBASites/PDFs/2014CallReportSurveyResults.pdf

We also encourage the Federal Reserve to streamline the FRY-9 for shell holding companies of community banks. The current FRY-9 requires too much information in cases where the holding company has no other assets but the stock of the bank.

Small Bank Holding Company Policy Statement. Appendix C of Regulation Y includes the Small Bank Holding Company Policy Statement on Assessment of Financial and Managerial Factors (Policy Statement). This Policy Statement applies only to bank holding companies with pro forma consolidated assets of less than $500 million that (1) are not engaged in any nonbanking activities involving significant leverage and (2) do not have a significant amount of outstanding debt that is held by the general public.

ICBA strongly believes that the asset threshold under the Policy Statement should be raised to at least $5 billion. In addition, we recommend the debt-to-equity ratio threshold of 1:1 be increased to 3:1. Increasing the exemption to $5 billion would improve the ability of small local institutions to sell their stock locally, keeping the financial decisions affecting the community in the local area.

Access to capital for community banks has never been more difficult than it is today. Since 2007, the public capital markets have been either unavailable or unattractive to many community bank and holding companies. Many community banks have had to rely more on existing shareholders, directors and insiders for capital raises and less on new investors, including institutions and private equity investors. Furthermore, many community banks will need to raise additional capital not only for business purposes but also to ensure compliance with regulatory requirements including the new Basel III requirements. Those community banks that have not redeemed their Troubled Asset Relief Program (TARP) or Small business Lending Fund (SBLF) securities, or that have been deferring dividends on their trust preferred securities, have additional reasons for needing capital.

Allowing a larger number of community bank holding companies to qualify under the Policy Statement (i.e., those with consolidated assets of up to at least $5 billion) would make it easier for these community bank holding companies to issue debt and equity on an unconsolidated basis that could be used to support the capital needs of their banking subsidiaries or to redeem their TARP or SBLF securities. We also believe a 3:1 debt to equity ratio is a reasonable holding company leverage ratio and would also facilitate the raising of capital at the holding company level. Small savings and loan holding companies should also have the ability to benefit from using the Policy Statement.

De Novo Bank Applications. ICBA appreciates the meetings we have had with FDIC staff about de novo bank application process. However, we continue to hear from our members and others that FDIC policies and practices are inhibiting the formation of de novo institutions.

For example, it has been reported to us that the requirement that a state nonmember de novo bank is subject to FDIC approval for any material change or deviation in its business plan during the fourth through seventh years serves as a major deterrent to

1615 L Street NW, Suite 900, Washington, DC 20036-5623 | 800-422-8439 | FAX: 202-659-1413 | Email: info@icba.org | Website: www.icba.org

organizing groups and their efforts to raise sufficient capital in their communities. There are also reports that at pre-filing meetings with the FDIC, the organizers have been advised that they need to raise capital upfront in amounts sufficient to maintain a leverage ratio of at least 8 percent for a seven year period.

We have also heard from others that the increasingly lengthy and uncertain application process serves as a deterrent to forming de novo banks. Apparently, some would-be applicants are overwhelmed by the uncertainty of approval and timely processing of the applications, and thus decide not to take the considerable risk of subjecting themselves to those uncertainties.

Given the continuing dearth in de novo applications, ICBA urges the FDIC to streamline the application process. Furthermore, the FDIC should advise staff that meet with de novo bank applicants and process applications that it is not requiring initial capital to cover the full seven year period, that the application process will not overwhelm applicants, and that the FDIC will not question the judgment of the organizing group of the need for a de novo bank in the market unless it is clearly erroneous.

Also given the misperceptions surrounding the FDIC's policies and practices, **ICBA recommends that the FDIC issue a new Financial Institutions Letter or FIL to help dispel misconceptions and reaffirm the FDIC's support for the formation of de novo banks.**

Simplification and Update of Regulation O. Federal Reserve Regulation O still continues to confuse community bankers. The rules on prior approval of extensions of credit, on additional restrictions on loans to executive officers, and the definition of what is an "extension of credit" need to be clarified and simplified. Furthermore, it is time to revisit some of the loan limits, such as the $100,000 aggregate credit limit to executive officers in Section 215.5.

ICBA suggests also easing some of the requirements for community banks with CAMELS composite ratings of "1" or "2" and management ratings of not lower than "2." We also think that the agencies should issue a Regulation O summary chart to capture the limitations on loans to various types of insiders in an easy comprehensive way, with cross references to Federal Reserve Regulation W.

Conclusion

ICBA hopes that this EGRPRA review process will be more of a success than the last one which failed to make any substantive changes to banking regulations. We strongly recommend that as part of the current EGRPRA process (1) the agencies hold at least six outreach meetings to solicit the comments and testimony of community banks to the regulatory burden, (2) the agencies establish an EGRPRA.gov website to post the comments received and list those regulations that community banks consider the most burdensome, and (3) establish an "EGRPRA czar" who could resolve interagency disputes over the regulations. But more importantly, a strong commitment at the top is

1615 L Street NW, Suite 900, Washington, DC 20036-5623 | 800-422-8439 | FAX: 202-659-1413 | Email: info@icba.org | Website: www.icba.org

needed to do what is necessary to eliminate regulation that is outdated, unnecessary or unduly burdensome. Otherwise, the whole EGRPRA process will be a meaningless, regulatory check-the-box exercise.

The overall regulatory burden has increased dramatically since 2007 when the last EGRPRA report was issued and when the EGRPRA director, John Reich, expressed his concerns about the future of community banking. We encourage the regulators to conduct their own empirical research confirming what other studies are showing—that community banks are exiting the business because the regulatory burden is so severe.

ICBA has a number of burden-reducing recommendations concerning the first two categories of regulations. With regard to call reports, we urge the agencies to adopt a streamlined call reporting system that would allow highly rated, well-capitalized community banks to file a short-form call report covering the first and third quarters and a long-form call report for the second and fourth quarters of each year. This would greatly reduce the call report burden.

ICBA also recommends amendment of the Small Bank Holding Company Policy Statement so that bank holding companies with consolidated assets of up to $5 billion could benefit from it. In addition, we recommend the debt-to-equity ratio threshold under the Policy Statement of 1:1 be increased to 3:1. Increasing the exemption to $5 billion and easing the leverage ratio would improve the ability of small local institutions to sell their stock locally and would allow them to more easily issue debt at the holding company level to support the capital needs of their banking subsidiaries.

ICBA still hears from our members and others that FDIC policies and practices are inhibiting the formation of de novo institutions. We believe the process should be streamlined and urge the FDIC to issue a FIL to help dispel misconceptions and reaffirm the FDIC's support for the formation of de novo banks.

ICBA also supports the simplification of Regulation O and recommends that the requirements be eased for those community banks with high management and CAMELS ratings. Some of the loan limits should be reviewed and updated, and the regulators should issue a simplified summary of the regulation for community banks.

ICBA appreciates the opportunity to comment on the first notice that was published by the banking agencies under EGRPRA to help identify those regulations in the first three categories of regulations that are outdated, unnecessary or unduly burdensome and to discuss the EGRPRA process and the regulatory burden on community banks. If you have any questions or would like additional information, please do not hesitate to contact me by email at Chris.Cole@icba.org.

Sincerely,
/s/ Christopher Cole
Christopher Cole
Executive Vice President and Senior Regulatory Counsel

PREPARED STATEMENT OF ED TEMPLETON

PRESIDENT AND CEO, SRP FEDERAL CREDIT UNION
ON BEHALF OF THE NATIONAL ASSOCIATION OF FEDERAL CREDIT UNIONS

FEBRUARY 12, 2015

Introduction

Good Morning, Chairman Shelby, Ranking Member Brown and Members of the Committee. My name is Ed Templeton and I am testifying today on behalf of the National Association of Federal Credit Unions (NAFCU). I serve as the President and CEO of SRP Federal Credit Union, headquartered in North Augusta, South Carolina. I have over 42 years of financial industry experience, including the last 27 years as President and CEO of SRP FCU. SRP FCU is a community credit union serving over 104,000 members in several counties in South Carolina along the Georgia border with nearly $700 million in assets.

I currently serve as a Director-at-large and Chairman of NAFCU's Board of Directors. I have served in a number of roles with the Association while on the Board, including as Vice-Chairman and a member of the Legislative Committee. I received my BBA from Augusta College, graduated from the Georgia School of Banking and the BAI School of Bank Administration at the University of Wisconsin.

As you are aware, NAFCU is the only national organization exclusively representing the interests of the Nation's federally chartered credit unions. NAFCU-member credit unions collectively account for approximately 69 percent of the assets of all federally chartered credit unions. NAFCU and the entire credit union community appreciate the opportunity to participate in today's hearing regarding regulatory relief for credit unions.

Historically, credit unions have served a unique function in the delivery of essential financial services to American consumers. Established by an Act of Congress in 1934, the Federal credit union system was created, and has been recognized, as a way to promote thrift and to make financial services available to all Americans, many of whom may otherwise have limited access to financial services. Congress established credit unions as an alternative to banks and to meet a precise public need—a niche that credit unions still fill today.

Every credit union, regardless of size, is a cooperative institution organized "for the purpose of promoting thrift among its members and creating a source of credit for provident or productive purposes." (12 USC 1752(1)). While over 80 years have passed since the Federal Credit Union Act (FCUA) was signed into law, two fundamental principles regarding the operation of credit unions remain every bit as important today as in 1934:

- credit unions remain wholly committed to providing their members with efficient, low-cost, personal financial service; and,
- credit unions continue to emphasize traditional cooperative values such as democracy and volunteerism.

These principles apply for all credit unions, regardless of their size. When compared with the Nation's "Too Big To Fail" financial institutions, all credit unions are "small" institutions. It is with this fact in mind that NAFCU believes that there should not be artificial or arbitrary asset thresholds established for which size credit unions should receive regulatory relief. The challenges facing the industry impact, or stand to impact, all credit unions and all ultimately need relief.

Today's hearing is an important one and the entire credit union community appreciates the opportunity to expand on the topic of regulatory relief. In my testimony I will cover several main points, including:

- **Increased regulatory burden and how it is impacting credit unions;**
- **The importance of legitimate cost-benefit analysis at the regulatory agencies from the onset;**
- **Understanding risk in the financial system and the potential of regulating credit unions out of existence with one-size fits all regulatory solutions;**
- **How Congress can provide regulatory relief; and**
- **How the regulatory agencies can provide regulatory relief.**

I. Increased Regulatory Burden has Impacted Credit Unions

Credit unions have a long track record of helping the economy grow and making loans when other lenders have left various markets. This was evidenced during the recent financial crisis when credit unions kept making auto loans, home loans, and

small business loans when other lenders cut back. Still, credit unions have always been some of the most highly regulated of all financial institutions, facing restrictions on who they can serve and their ability to raise capital.

Credit union lending continues to grow at a solid pace today, up about 18 percent as of June 2014, as compared to 2009. Although credit unions continue to focus on their members, the increasing complexity of the regulatory environment is taking a toll on the credit union industry. While NAFCU and its member credit unions take safety and soundness extremely seriously, the regulatory pendulum post-crisis has swung too far toward an environment of over regulation that threatens to stifle economic growth. As the National Credit Union Administration (NCUA) and the Consumer Financial Protection Bureau (CFPB) work to prevent the next financial crisis, even the most well intended regulations have the potential to regulate our industry out of business.

During the consideration of financial reform, NAFCU was concerned about the possibility of over regulation of good actors such as credit unions, and this is why NAFCU was the only credit union trade association to oppose the CFPB having rulemaking authority over credit unions. Unfortunately, many of our concerns about the increased regulatory burdens that credit unions would face under the CFPB have proven true. While there may be credible arguments to be made for the existence of a CFPB, its primary focus should be on regulating the unregulated bad actors, not adding new regulatory burdens to good actors like credit unions that already fall under a prudential regulator. As expected, the breadth and pace of CFPB rulemaking is troublesome, and the unprecedented new compliance burden placed on credit unions has been immense. While it is true that credit unions under $10 billion are exempt from the examination and enforcement from the CFPB, all credit unions are subject to the rulemakings of the agency and they are feeling this burden. While the CFPB has the authority to exempt certain institutions, such as credit unions, from agency rules, they have been lax to use this authority to provide relief.

The impact of this growing compliance burden is evident as the number of credit unions continues to decline, dropping by 22 percent (more than 1,700) institutions since 2007. A main reason for the decline is the increasing cost and complexity of complying with the ever-increasing onslaught of regulations. Since the 2nd quarter of 2010, we have lost 1,100 federally insured credit unions, 96 percent of which were smaller institutions below $100 million in assets. Many smaller institutions simply cannot keep up with the new regulatory tide and have had to merge out of business or be taken over. Credit unions need regulatory relief, both from Congress and their regulators.

This growing demand on credit unions is demonstrated by a 2011 NAFCU survey of our membership that found that nearly 97 percent of respondents were spending more time on regulatory compliance issues than they did in 2009. A 2012 NAFCU survey of our membership found that 94 percent of respondents had seen their compliance burdens increase since the passage of the Dodd-Frank Act in 2010. At SRP FCU our compliance costs have more than doubled since 2009 and we are adding another compliance officer in 2015 just to keep up. Many credit unions find themselves in the same situation, as a March, 2013, survey of NAFCU members found that nearly 27 percent had increased their full-time equivalents (FTEs) for compliance personnel in 2013, as compared to 2012. That same survey found that over 70 percent of respondents have had noncompliance staff members take on compliance-related duties due to the increasing regulatory burden. This highlights the fact that many noncompliance staff are being forced to take time away from serving members to spend time on compliance issues.

At SRP FCU we have felt the pain of these burdens as well. There are costs incurred each time a rule is changed and most costs of compliance do not vary by size, therefore it is a greater burden on credit unions like mine. We are required to update our forms and disclosures, reprogram our data processing systems and retrain our staff each time there is a change, just as large institutions are. Unfortunately, lending regulation revisions never seem to occur all at once. If all of the changes were coordinated and were implemented at one time, these costs would have been significantly reduced and a considerable amount of our resources that were utilized to comply could have been used to benefit our members instead.

If Congress and the regulators will not act to provide regulatory relief to credit unions, the industry may look vastly different a decade from now.

II. Credit Unions Need Regulatory Relief

Regulatory burden is the top challenge facing all credit unions. While smaller credit unions continue to disappear from the growing burden, all credit unions are finding the current environment challenging. Finding ways to cut-down on burdensome and unnecessary regulatory compliance costs is the only way for credit unions

to thrive and continue to provide their member-owners with basic financial services and the exemplary service they need and deserve. It is also a top goal of NAFCU.

Ongoing discussions with NAFCU member credit unions led to the unveiling of NAFCU's initial "Five Point Plan for Regulatory Relief" in February, 2013, and a call for Congress to enact meaningful legislative reforms that would provide much needed assistance to our Nation's credit unions. The need for regulatory relief is even stronger in 2015, which is why we are releasing an updated version of the plan for the 114th Congress.

The 2015 plan calls for relief in five key areas: (1) Capital Reforms for Credit Unions, (2) Field of Membership Improvements for Credit Unions, (3) Reducing CFPB Burdens on Credit Unions, (4) Operational Improvements for Credit Unions, and (5) 21st Century Data Security Standards.

Recognizing that there are a number of outdated regulations and requirements that no longer make sense and need to be modernized or eliminated, NAFCU also compiled and released a document entitled "NAFCU'S Dirty Dozen" list of regulations to remove or amend in December of 2013 that outlined 12 key regulatory issues credit unions face that should be eliminated or amended. While some slight progress was made on several of these recommendations, we have updated that list for 2015 to outline the "Top Ten" regulations that regulators can and should act on now to provide relief. This list includes:

1. Improving the process for credit unions seeking changes to their field of membership;
2. Providing More Meaningful Exemptions for Small Institutions;
3. Expanding credit union investment authority;
4. Increasing the number of Reg D transfers allowed;
5. Additional regulatory flexibility for credit unions that offer member business loans;
6. Updating the requirement to disclose account numbers to protect the privacy of members;
7. Updating advertising requirements for loan products and share accounts;
8. Improvements to the Central Liquidity Facility (CLF);
9. Granting of waivers by NCUA to a Federal credit union to follow a state law; and
10. Updating, simplifying and making improvements to regulations governing check processing and fund availability.

In my statement today, we will highlight a number of key issues where these regulatory burdens and proposals are posing immediate threats to the ability of credit unions to serve their members and give them the financial products that they want and need. Perhaps one of the greatest challenges credit unions face is the often times grossly distorted time and cost estimates provided to them by the regulatory agencies in the proposal stages of rulemaking. As will be further discussed in my testimony below, regardless of whether or not the estimates are put forward in good faith, there continues to be a major disconnect between the regulatory agencies in Washington, D.C., and credit unions across the country in terms of how time consuming, costly, and problematic it can be to implement various proposals. Additionally, there isn't always a great amount of thought given to the actual operational aspects of many proposals including how they will interact with existing regulations and how they would address risk in the system without layering needless regulation upon needless regulation.

III. Recent Actions to Provide Relief

NAFCU and the entire credit union community would like to thank the Members of this Committee and your staffs for all of your work on the passage of H.R. 3468, the *Credit Union Share Insurance Fund Parity Act* in the 113th Congress. As you are aware, this legislation allows NCUA to provide pass-through share insurance coverage on Interest on Lawyers Trust Accounts (IOLTAs) and other similar accounts, similar to what the Federal Deposit Insurance Corporation (FDIC) provides. We also appreciate the passage of the *American Savings Promotion Act.*

NAFCU also recognizes that there has been effort by regulators, such as NCUA and CFPB to provide relief via the regulatory process. While there have been some small steps taken, too often regulators set arbitrary asset thresholds for relief and don't actually consider the risk or complexities of institutions. Regulation of the system should match the risk to the system. As previously noted, when compared with the Nation's "Too Big To Fail" financial institutions, all credit unions are "small" institutions and not very complex. There should not be artificial or arbitrary asset

thresholds established for which size credit unions should receive regulatory relief. The challenges facing the industry impact, or stand to impact, all credit unions and all ultimately need relief.

More needs to be done. In particular, NAFCU is also concerned that regulators sometimes try to frame new costly and burdensome proposals as "regulatory relief" when the end result for credit unions is higher costs for little relief. One example is NCUA's request for additional third-party vendor examination authority for credit unions which they have called "regulatory relief."

NAFCU does not support spending credit union resources to expand NCUA's examination authority into noncredit union third parties. While NCUA contends that examination and enforcement authority over third-party vendors will provide regulatory relief for the industry, NAFCU and our members firmly believe that such authority is unnecessary and will require considerable expenditure of the agency's resources and time. NAFCU disagrees with the assertion that third-party vendor examination and enforcement authority will provide any significant improvement to credit union safety and soundness. The key to success with appropriate management of vendors is due diligence on behalf of the credit union. NAFCU supports credit unions being able to do this due diligence and NCUA already offers due diligence guidance to credit unions. Giving NCUA additional authority will require an additional outlay of agency resources, which will in turn necessitate higher costs to credit unions.

Another prime example of a proposal NCUA has called relief, but is in fact a new heavy burden on the industry, is the agency's current proposal for a risk-based capital system for credit unions.

IV. NCUA's 2nd Risk-Based Capital Proposal: Still a Solution in Search of a Problem

On January 15, 2015, the National Credit Union Administration (NCUA) Board, in a 2–1 vote, issued a revised risk-based capital proposed rule for credit unions. NAFCU has just begun to analyze the proposal and will be providing NCUA with detailed comments and concerns from our membership as part of the agency's request for comment before the April 27, 2015, deadline. We are encouraged to see that the revised version of this proposal addresses some changes sought by our membership. However, NAFCU maintains that this costly proposal is unnecessary and will ultimately unduly burden credit unions and the communities they serve.

A Costly Experiment for Credit Unions

NAFCU and its member credit unions remain deeply concerned about the cost of this proposal. NAFCU's analysis estimates that credit unions' capital cushions (a practice encouraged by NCUA's own examiners) will suffer over a $470 million hit if NCUA promulgates separate risk-based capital threshold for well capitalized and adequately capitalized credit unions (a "two-tier" approach). Specifically, in order to satisfy the proposal's "well-capitalized" thresholds, today's credit unions would need to hold at least an additional $729 million. On the other hand, to satisfy the proposal's "adequately capitalized" thresholds, today's credit unions would need to hold at least an additional $260 million. Despite NCUA's assertion that only a limited number of credit unions will be impacted, this proposal would force credit unions to hold hundreds of millions of dollars in additional reserves to achieve the same capital cushion levels that they currently maintain. These are funds that could otherwise be used to make loans to consumers or small businesses and aid in our Nation's economic recovery.

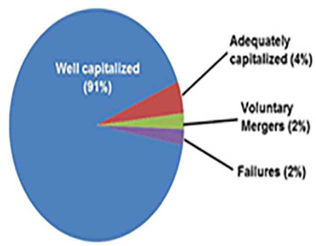
In addition, NCUA's own direct cost estimate approximates that is will cost $3.75 million for the agency to adjust the Call Report, update its examination systems and train internal staff to implement the proposed requirements. NCUA also estimates credit unions would incur an ongoing $1.1 million expense to complete the adjusted Call Report fields. NCUA's conservative estimate states that it will only take a meager 40 hours to completely review the 450-page proposal against a credit union's current policies at a cost of over $5.1 million. We expect that the true costs will be much higher when credit unions have to comply.

Impact Analysis

NCUA estimates that 19 credit unions would be downgraded if the new risk-based proposal were in place today. NAFCU believes the real impact is best illustrated with a look at its implications during a financial downturn. Under the new proposal, the number of credit unions downgraded more than doubles during a downturn in the business cycle. Because the nature of the proposal is such that, in many cases, assets that would receive varying risk weights under the proposal are grouped into the same category on NCUA call reports, numerous assumptions must be made to estimate impact.

Under our most recent analysis, NAFCU believes 45 credit unions would have been downgraded during the financial crisis under this proposal. Of those 45, 41 of credit unions would be well-capitalized today. To have avoided downgrade, the institutions would have had to increase capital by $145 million, or an average $3.2 million per institution. As the chart on the next page demonstrates, almost all of the credit unions that would have been downgraded—95 percent—are well capitalized or adequately capitalized today *without NCUA's risk-based capital proposal being needed.*

Current status of the credit unions that would have been downgraded in 2009 under RBC2



Source: NCUA call report data

Legal Authority

NAFCU strongly believes that NCUA lacks the statutory authority to prescribe a separate risk-based capital threshold for well capitalized and adequately capitalized credit unions. NCUA Board Member J. Mark McWatters, the dissenting vote on the proposal, called NCUA's lack of legal authority the most "fundamental issue presented before the Board." The Federal Credit Union (FCU) Act expressly provides that NCUA shall implement a risk-based net worth requirement that "take[s] account of any material risk against which the net worth ratio required for an insured credit union to be *adequately capitalized* may not provide adequate protection." 12 U.S.C. § 1790d(d). The FCU Act does not provide NCUA the express authority to implement a separate risk-based net worth threshold for the "well capitalized" net worth category. Simply put, Congress has not expressly authorized the Board to adopt a two-tier risk-based net worth standard.

Further, it has been disclosed that NCUA authorized the expenditure of $150,000 to seek an outside legal opinion over the legality of the risk-based proposal. It is worth noting that NCUA continued forward with this proposal despite the neutrality of the outside opinion which recognized the questionable legal standing of the proposal by noting only that a court "could" conclude that NCUA had the statutory authority to offer a two-tier system.

Legislative Change

Ultimately, NAFCU believes legislative changes are necessary to bring about comprehensive capital reform for credit unions such as allowing credit unions to have access to supplemental capital sources, and making the statutory changes necessary to design a true risk-based capital system for credit unions that gives greater statutory flexibility in determining corresponding leverage ratio standards.

V. Credit Unions Need Field of Membership Help

In addition to the legislative changes needed on the capital front for credit unions, field of membership (FOM) rules for credit unions need to be modernized, both on the legislative front and by NCUA.

NAFCU believes reasonable improvements to current field-of-membership restrictions include: (1) streamlining the process for converting from one charter type to another; (2) updating and revising population limits in NCUA's field of membership rules; and, (3) making statutory changes to make it easier for all credit unions to add "underserved" areas within their field of membership or continuing serving their current select employee groups (SEGs) when they change charters. Additionally, NAFCU believes that NCUA should have a "reverse wild card" authority where Federal credit unions can request a waiver from the agency that allows them to follow a State rule for credit unions if it allows them to serve their members better.

Charter Conversions

NAFCU continues to hear from our members that NCUA's Rules and Regulations governing charter conversions for credit unions that seek to convert from one type of Federal charter to another are unnecessarily cumbersome. We ask that NCUA review its rules on conversions and initiate a rulemaking for changes, with particular focus on conversions to a community charter.

NAFCU and our members strongly oppose the agency's chartering rule that prevents a single- or multi-associational chartered Federal credit union (FCU) from continuing to serve its existing field of membership when it converts to a community charter, unless the field of membership is entirely within the new community. The effect of this limitation has been that FCUs are dissuaded from offering their services to more people, a result that we do not believe is desirable.

Definition of "Rural District"

Under NCUA's Rules and Regulations, a "rural district" is defined as (1) a district that has well-defined, contiguous geographic boundaries; (2) more than 50 percent of the district's population resides in census blocks or other geographic areas that are designated as rural by the United States Census Bureau; and (3) does not exceed certain other population thresholds. The district's population cannot exceed either (a) the greater of 250,000 or 3 percent of the population of the State in which the majority of the district is located, or (b) if the district has well-defined contiguous geographic boundaries, it does not have a population density in excess of 100 people per square mile, and the total population of the district does not exceed the greater of 250,000 or 3 percent of the population of the State in which the majority of the district is located.

The current definition of "rural district" was revised in February, 2013. As NAFCU has expressed many times to NCUA, it is important that the definition not be overly restrictive and consequently deprive many Americans the opportunity to receive high quality financial services from a credit union.

While NAFCU welcomed NCUA's efforts to enable more credit unions to obtain a community charter under the "rural district" designation, we continue to hear from our members that the final rule has had only a limited effect. We urge the agency to reconsider the definition of "rural district" so as to provide greater flexibility for credit unions that would like to serve rural areas of our Nation. A more flexible definition of "rural district" would increase credit availability to those who might otherwise not have ready access to financial services.

NAFCU notes that under the "three percent option" only those credit unions that seek to serve in rural areas in the 13 most populated States in the country have been affected by the final rule. Those credit unions that would like to serve persons who live in rural areas in the remaining 37 States and U.S. Territories remain subject to an arbitrary 250,000 population limit.

NAFCU is also concerned with the final rule's 250,000 population limit. In prior communications with the agency, we urged NCUA to, at the very least increase this limit to the pre-2010 level of 500,000, which was reduced without explanation. With the 2010 changes, the agency effectively decided that a "rural district" is actually 60 percent smaller in population than it previously thought. This fact, in and of itself, is troubling. NAFCU believes the 250,000 limit is arbitrary and does not pass even a cursory review of our Nation's makeup. We urge the agency to reconsider this threshold.

Further, NAFCU believes NCUA should either remove or greatly increase the 100 person per square mile limit, as this population density threshold is far too low. NAFCU does not believe a person-per-square mile limitation should be part of the analysis for determining whether a credit union should be granted a community charter with "rural district" designation.

Statutory Changes are Needed

Congress can provide FOM relief by removing outdated restrictions that credit unions face such as expanding the criteria for defining "urban" and "rural" and allowing voluntary mergers involving multiple common bond credit unions and allowing credit unions that convert to community charters to retain their current select employee groups (SEGs).

Furthermore, Congress should clarify that all credit unions, regardless of charter type, should be allowed to add underserved areas to their field of membership. This is an important issue for SRP FCU, as our membership includes Allendale and Barnwell counties which are some of the most rural in South Carolina. They are also some of the poorest, with large percentages living below the poverty level. SRP FCU has a strong presence in these counties, with a significant amount of the adult populations in those counties being members. We would like to take our success in

these counties and help other underserved communities. However, as a community charter, we cannot add underserved areas to our field of membership.

VI. Regulators Must Be Held Accountable for Cost and Compliance Burden Estimates

Cost and time burden estimates issued by regulators such as NCUA and CFPB are often grossly understated. Unfortunately, there often is never any effort to go back and review these estimates for accuracy once a proposal is final. We believe Congress should require periodic reviews of "actual" regulatory burdens of finalized rules and ensure agencies remove or amend those rules that vastly underestimated the compliance burden. A March, 2013, survey of NAFCU's membership found that over 55 percent of credit unions believe compliance cost estimates from NCUA and the CFPB are lower than they are when the credit union actual has to implement the proposal.

We believe Congress should use their oversight authority to require regulators to provide specific details on how they determined their assumptions in their cost estimates when submitting those estimates to OMB and publishing them in proposed rules. It is important that regulators be held to a standard that recognizes burden at a financial institution goes well beyond additional recordkeeping. At SRP FCU, we spend approximately 116 employee hours to fill out one NCUA Call Report. NCUA's 2014 submission to OMB estimates the time to complete the Call Report to be 6.6 hours per reporting cycle. Something is amiss. That's 109 hours of regulatory burden that are not being recognized on just one form. With the requirements of the new proposed risk-based capital proposal, this burden is likely to get worse. More needs to be done to force regulators to justify that the benefits of a proposal outweigh its costs.

VII. Revisiting Legislation from the 113th Congress to Provide Relief

There were a number of measures introduced in either the House or Senate in the 113th Congress to provide credit unions with regulatory relief. Unfortunately, many of these measures stalled at various points in the legislative process. Still, we hope that these measures gain traction in the 114th Congress:

Regulatory Relief for Credit Unions Act of 2013

The *Regulatory Relief for Credit Unions Act of 2013* (H.R. 2572) reflected several provisions important to NAFCU. The legislation would:

- establish a risk-based capital system for credit unions;
- allow NCUA to grant Federal credit unions a waiver to follow a State rule instead of a Federal one in certain situations;
- authorize NCUA to step in where appropriate to modify a CFPB rule affecting credit unions;
- require that NCUA and CFPB revisit cost/benefit analyses of rules after 3 years so they have a true sense of the compliance costs for credit unions;
- require NCUA to conduct a study of the Central Liquidity Facility and make legislative recommendations for its modernization;
- give credit unions better control over their investment decisions and portfolio risk.

Member Business Lending Improvements

Senators Mark Udall and Rand Paul introduced S. 968, the *Small Business Lending Enhancement Act of 2013,* and Representatives Royce and McCarthy introduced H.R. 688, the *Credit Union Small Business Jobs Creation Act.* Both bills would raise the arbitrary cap on credit union member business loans from 12.25 percent to 27.5 percent of total assets for credit unions meeting strict eligibility requirements.

Additionally, NAFCU supported legislation (H.R. 4226) to exclude loans made to non-owner occupied 1- to 4-family dwelling from the definition of a member business loan and legislation (H.R. 5061) to exempt loans made to our Nation's veterans from the definition of a member business loan.

Furthermore, NAFCU also supports exempting from the member business lending cap loans made to nonprofit religious organizations, businesses with fewer than 20 employees, and businesses in "underserved areas."

Supplemental Capital for Credit Unions

Allowing eligible credit unions access to supplemental capital, in addition to retained earning sources, will help ensure healthy credit unions can achieve manageable asset growth and continue to serve their member-owners efficiently as the country recovers from the financial crisis.

During the last Congress Representatives King and Sherman introduced H.R. 719, the *Capital Access for Small Businesses and Jobs Act,* a bill that would authorize NCUA to allow Federal credit unions to receive payments on uninsured, nonshare capital accounts, provided the accounts do not alter the cooperative nature of the credit union. The need for supplemental capital is even greater today as the NCUA pushes ahead with their stringent risk-based capital proposal.

Reforms to the definition of "Points and Fees"

Senators Manchin, Johanns, Toomey, Kirk, Stabenow and Levin introduced S. 1577, *The Mortgage Choice Act,* a bipartisan bill that would exclude affiliated title charges from the "points and fees" definition, and clarify that escrow charges should be excluded from any calculation of "points and fees." These important changes would greatly improve the definition of "points and fees" used to determine whether a loan meets the QM test, and would ensure that those with low and moderate means would continue to be able to obtain their mortgages from their credit union at a reasonable price. We appreciate the leadership of the sponsors of this legislation and urge the Senate to advance this issue as soon as possible. Similar legislation (H.R. 685) was just reintroduced in the House last week.

Privacy Notices

Earlier this week Senators Moran and Heitkamp reintroduced bipartisan legislation (S. 423) that would remove the requirement that financial institutions send redundant paper annual privacy notices if they do not share information and their policies have not changed, provided that they remain accessible elsewhere. These duplicative notices are costly for the financial institution and often confusing for the consumer as well. In the 113th Congress, this legislation had over 70 cosponsors in the Senate. We appreciate the continued leadership on this important issue. Similar legislation has been introduced in the House this Congress as H.R. 601.

Examination Fairness

Credit unions face more examiner scrutiny than ever, as the examination cycles for credit unions have gone from 18 months to 12 months since the onset of the financial crisis even though credit union financial conditions continue to improve. Additional exams mean additional staff time and resources to prepare and respond to examiner needs. NAFCU has concerns about the continued use of Documents of Resolution (DOR) when they are not necessary or are used in place of open and honest conversations about examiner concerns. A survey of NAFCU members last year found that nearly 40 percent of credit unions that received DORs during their last exam felt it was unjustified and nearly 15 percent of credit unions said their examiners appeared less competent than in the past. NAFCU supports effective exams that are focused on safety and soundness and flow out of clear regulatory directives and later in my testimony we will outline areas where we think NCUA can do more.

NAFCU strongly supported legislation introduced (S. 727) by Senators Manchin and Moran last Congress that would have helped to ensure timeliness, clear guidance and an independent appeal process free of examiner retaliation. Identical legislation (H.R. 1553) was introduced in the House and NAFCU is hopeful that both chambers take this issue up during the 114th Congress.

Relief From the Consumer Financial Protection Bureau

NAFCU has consistently supported measures in both chambers to bring greater accountability and transparency to the Consumer Financial Protection Bureau (CFPB) including replacing the director with a board akin to other Federal financial regulators, bringing the CFPB under the congressional appropriations process, and giving the Financial Stability Oversight Council additional tools to challenge CFPB rulemaking. NAFCU appreciates the leadership of Senators Fischer, Scott, Barrasso, Chambliss, Collins, Inhofe, Johnson and Roberts for spearheading these efforts.

Additionally, we appreciate the work of Senators Toomey and Donnelly for introducing S. 2732, the CFPB Examination and Reporting Threshold Act, to address the arbitrary $10 billion threshold for examination of depository institutions by the CFPB. NAFCU believes that all credit unions, as good actors during the financial crisis, should be exempt from being subject to the CFPB and would support adding language to the legislation *exempting all credit unions* in place of the proposed $50 billion threshold.

Relief From Operation Choke Point

The Operation Choke Point initiative was launched in an effort to fight consumer fraud by denying fraudulent businesses access to banking services and holding financial institutions and third-party processors accountable if they continue to serve a client operating in a fraudulent manner. NAFCU, with many others in the finan-

cial services industry, has noted concerns that this program "could seriously deter the natural growth and development of e-commerce and stifle future economic growth."

In the House, Representative Leutkemeyer introduced H.R. 4986, the End Operation Choke Point Act, a bill that would create a legal safe harbor for financial institutions, including credit unions that meet qualifying criteria. Luetkemeyer also introduced H.R. 5758, the Financial Institution Customer Protection Act, a bill that would rein in the Justice Department's "Operation Choke Point" initiative by restricting its ability to order the termination of accounts in financial institutions by requiring Federal banking regulators, to provide material reason beyond reputational risk for ordering a financial institutions to terminate a banking relationship. It would also require regulators to put any order to terminate a customer's account into writing. The latter bill was reintroduced last week in substantially similar form and under the same title as H.R. 766.

Helping Expand Lending Practices in Rural Communities Act

Introduced by Leader McConnell (S. 1916), this bill would be helpful to small creditors, including credit unions, as they deal with the CFPB's definition "rural area" particularly as it relates to the ability-to-repay rule. Representative Andy Barr (H.R. 2672) had a similar bill in the House and NAFCU hopes these bicameral efforts continue this Congress. As I outline in my testimony below, NAFCU also has concerns with how NCUA defines "rural."

Community Bank Mortgage Servicing Asset Capital Requirements Study Act

Introduced by Representatives Luetkemeyer and Perlmutter as H.R. 4042 in the last Congress, this bill would delay the implementation of Basel III regulations on mortgage servicing assets until an impact study is conducted and alternatives are explored. Given the circumstances credit unions find themselves in with the risk-based capital proposal, NAFCU believes this is an appropriate vehicle to include a similar analysis be done by the NCUA pertaining to their risk-based capital proposal.

SAFE Act Confidentiality and Privilege Enhancement Act

Introduced by Chairman Capito as H.R. 4626 in the House last Congress, the bill would clarify the confidentiality of information shared between State and Federal financial service regulators under the S.A.F.E. Mortgage Licensing Act. This commonsense technical fix is welcomed by credit unions as it applies to the Nationwide Mortgage Licensing System & Registry established as an oversight mechanism to collect information from Mortgage Loan Originators. Senator Capito just reintroduced this last week and we applaud her efforts.

VIII. Areas Where Regulators Can Provide Relief to Credit Unions

While my testimony has outlined important issues impacting credit unions and highlighted steps that Congress can take to help, there are additional steps that the NCUA, CFPB, FHFA, the Federal Reserve and others can currently take to provide relief without congressional action and we would encourage them to do so.

NCUA

We are pleased that the National Credit Union Administration has been willing to take some small steps recently to provide credit unions relief. A prime example of this is the agency's proposed fixed-asset rule. This is a topic that was previously on NAFCU's "Dirty Dozen" and we are hopeful that the agency will continue moving forward and finalize this proposal.

We are also glad to see NCUA's voluntary participation in review of its regulations pursuant to the *Economic Growth and Regulatory Paperwork Reduction Act of 1996* (EGRPRA). This review provides an important opportunity for credit unions to voice their concerns about outdated, unnecessary or unduly burdensome requirements of NCUA's Rules and Regulations.

While these small steps by NCUA are positive, NAFCU believes that a big part of the problem is the cumulative impact of numerous regulations. While NCUA is not required to follow the President's Executive Order 13563—Improving Regulation and Regulatory Review, we believe that the agency should adhere to the spirit of it during the rulemaking process, such as taking into account the costs of cumulative costs of its regulations on the credit union industry. As noted earlier, NAFCU believes all credit unions need relief and regulators such as NCUA should not solely rely on an arbitrary asset-size threshold when providing relief.

While my testimony has already outlined key areas such as field of membership, risk-based capital and compliance burden estimates, there are a number of areas where we would like to see NCUA action to provide relief.

Member Business Lending

A major area where we think NCUA can use its authority to provide relief is with member business lending. The Member Business Lending (MBL) regulation, as NAFCU and our members have consistently maintained, is far too restrictive and cumbersome.

As NAFCU outlined in both its March 5, 2014, letter to NCUA Board and our "Top Ten" list of regulations to eliminate or amend, there are several aspects of the MBL requirements which should be improved, including: changes to the waiver requirements and waiver process to make it more efficient and easier to obtain individual and blanket waivers; expanding opportunities to obtain waivers; and removing the 5 year relationship requirement to obtain a personal guarantee waiver. Additionally, NCUA should use its authority granted in the FCU Act to provide an exception to the limitations on member business loans (the MBL cap) for those credit unions that have a history of making MBLs to their members for a period of time.

Section 1757a of the FCU Act contains the limitations on MBLs. Under Part 723 of NCUA's Rules and Regulations, the aggregate MBL limit for a credit union is limited to the lesser of 1.75 times the credit union's net worth or 12.25 percent of the credit union's total assets. However, the FCU Act also contains exceptions to the MBL cap. In particular, it provides exception authority from the MBL cap for "an insured credit union chartered for the purpose of making, or that has a history of primarily making, member business loans to its members, as determined by the Board." *See,* 12 U.S.C. § 1757a(b)(1).

Traditionally, this provision in § 1757a has been construed narrowly by NCUA. Section 723.17(c) of NCUA's Rules and Regulations currently defines credit unions that have a history of primarily making member business loans as credit unions that have either 25 percent of their outstanding loans in member business loans or member business loans comprise the largest portion of their loan portfolios, as evidenced by any Call Report or other document filed between 1995 and 1998. NAFCU continues to hear from our members that this definition is overly restrictive and often prevents them from extending sound loans to their small business members, many of whom have been abandoned by other financial institutions due to their smaller size.

NAFCU has urged NCUA to take a broader interpretation of the history of primarily making MBLs provision of the FCU Act. This can be done by NCUA utilizing its statutory authority to create an exception from the MBL cap for all credit unions that have a history of making MBLs for an extended period of time. NAFCU and our members believe that a credit union that has had a successful MBL program in place for a period of 5 years or greater would be a reasonable basis to satisfy this statutory authority.

NCUA has explained that the current definition "focuses on a credit union's historical behavior during the years leading up to the enactment of the *Credit Union Membership Access Act* (CUMAA)." NAFCU and our members believe this focus is unnecessarily restrictive, and we have urged the agency to expand the scope of the definition. NAFCU contends that it would be more appropriate for NCUA to consider a credit union's history of making MBLs in general, rather than restricting its focus solely to a credit union's behavior from 1995 through 1998. In particular, we believe the agency should define credit unions that have had a successful MBL program in place for at least 5 years as having a "history of primarily making MBLs." NAFCU has encouraged the NCUA Board to set this standard and make the exception available to all credit unions.

NCUA expanding the opportunities for credit unions to obtain waivers is another area where they could help. In February 2013, NCUA issued supervisory letter 13–01 to credit unions attempting to shed light on the criteria and processes for obtaining MBL waivers. While this guidance was useful to credit unions, NAFCU continues to hear from its members that the waiver process is complicated, slow moving, and inefficient. As a result, many credit unions have been unable to extend sound loans to their small business members, loans which may have been lost to competitors, or worse, never extended at all.

While waivers should not be used so frequently that they are the norm, the process to obtain one should not be so excessively difficult as to prevent credit unions from serving their membership effectively. Healthy, well-run credit unions with risk-focused MBL programs that maintain appropriate policies and procedures and that perform adequate due diligence on their member borrowers should be able to apply for and obtain blanket waivers which would help their membership.

Furthermore, the MBL regulations should be amended to expand a credit union's ability to obtain an individual or blanket waiver. Credit unions, because of their fundamental nature, are in a great position to extend credit to small businesses which will help fuel our Nation's economic recovery. Expansion of the waiver capa-

bilities would enable well run credit unions to extend loans to their small business members.

As noted above, the FCU Act contains the limitations on and exceptions to MBLs. However, the FCU Act does not prescribe limitations on the waivers that NCUA can put in place with regard to the regulations it imposes for MBLs that are not statutory requirements.

Section 723.10 of NCUA's Rules and Regulations contains an enumerated list of MBL-related requirements for which a credit union can apply for a waiver. NAFCU believes that this enumerated list of available waivers should be replaced with a more flexible waiver provision that would allow a credit union to apply for, and obtain, a waiver from a nonstatutorily required MBL regulatory requirement. The use of an enumerated list necessarily restricts a credit union from obtaining a waiver of a requirement which is not listed, even where such a waiver would not pose a safety and soundness concern to the credit union. NAFCU encourages NCUA to amend Section 723.10 to provide a more flexible waiver provision.

NCUA could issue appropriate guidance for the types of waivers that a credit union could obtain using a more flexible standard, which could include enumerated lists and appropriate examples. Section 723.11 of NCUA's Rules and Regulations contains the procedural requirements for a credit union to obtain a waiver, and it requires a credit union to submit a waiver request accompanied by a great deal of information related to the credit union's member business loan program. Under a more flexible provision, and taking into account safety and soundness considerations, NCUA should be able to determine from the information required to be provided pursuant to Section 723.11 whether a waiver is appropriate for a credit union. This approach would enhance a credit union's ability to provide MBLs to its members without compromising the safety and soundness of the credit union.

Budget Transparency

NCUA is funded by the credit unions it supervises. Each year, credit unions are assessed a different operating fee based on asset size. NCUA then pools the monies it receives from credit unions and uses those funds to create and manage an examination program. The monies that NCUA collects, however, have significantly increased over the past 6 years to cover a $109.7 million increase in the agency's budget during that period.

NAFCU supports the agency's efforts to accurately calculate the appropriate overhead transfer rate and urges NCUA to maintain a rate that is equitable to FCUs given they are funding the remaining agency expenses through operating fees. NAFCU encourages NCUA to continue to look for ways to decrease costs in order to reduce fees FCUs pay to the agency. In connection with this, NAFCU believes that credit unions deserve clearer disclosures of how the fees they pay the agency are managed.

As NAFCU has stated in previous communications to the agency, NCUA is charged by Congress to oversee and manage the National Credit Union Share Insurance Fund (NCUSIF), the Temporary Corporate Credit Union Stabilization Fund, the Central Liquidity Fund, and its annual operating budget. These funds are comprised of monies paid by credit unions. NCUA is charged with protecting these funds and using its operating budget to advance the safety and soundness of credit unions.

Because these funds are fully supported by credit union assets, NAFCU and our members strongly believe that credit unions are entitled to know how each fund is being managed. Currently, NCUA publicly releases general financial statements and aggregated balance sheets for each fund. However, the agency does not provide non-aggregated breakdowns of the components that go into the expenditures from the funds, such as the overhead transfer rate. Although NCUA releases a plethora of public information on the general financial condition of the funds, NAFCU urges the agency to fully disclose the amounts disbursed and allocated for each fund. For example, NAFCU and our members believe that NCUA should be transparent about how the monies transferred from the NCUSIF through the overhead transfer rate are allocated to the NCUA Operating Budget.

NCUA Board Member McWatters has urged greater transparency in NCUA's budget process, including an industry hearing on the budget. He has also outlined a series of recommendations for the agency to take to provide great budget transparency:

1. Additional detail regarding each of the following expenditures: Employee Pay and Benefits, Travel, Rent/Communications/Utilities, Administrative, and Contracted Services;

2. A detailed analysis of how NCUA may reduce the expenditures noted in item 1 above;
3. The submission of the methodology employed by NCUA in calculating the OTR for public comment, and a detailed description of the methodology adopted by NCUA following a thoughtful analysis of the comments received;
4. A detailed analysis of expenditures among NCUA, the National Credit Union Share Insurance Fund, the Temporary Corporate Credit Union Stabilization Fund, and the Central Liquidity Facility;
5. A detailed analysis of why NCUA's budget has increased by over 50-percent in the past 5 years, as well as a year-by-year analysis of all such increases;
6. A detailed analysis of all cost savings programs implemented by NCUA over the past 5 years;
7. A detailed analysis of all expenditures incurred by NCUA to support the Financial Stability Oversight Council (FSOC);
8. A detailed analysis of all expenditures incurred by NCUA in implementing the Sensitive Compartmented Information Facility (SCIF);
9. A detailed analysis of all expenditures that NCUA anticipates to incur with respect to the proposed risk based net worth rule, as well as all other proposed rules;
10. A formal cost-benefit analysis with respect to each rule or regulation proposed by NCUA, as well as a detailed description of the methodology employed by NCUA in conducting such analysis; and
11. A detailed reconciliation of how NCUA plans to allocate budget expenditures to achieve its strategic goals.

Many of these recommendations align with NAFCU's concerns and we would urge the Committee to call on the agency to implement these recommendations.

Advertising

Another area where NCUA could provide relief would be to amend its Rules and Regulations to accommodate for the rise of social media and mobile banking. Regulations governing advertising, such as 12 CFR 740.5, for example, contain requirements that are impossible to apply to social media and mobile banking, especially mediums that are interactive. A survey earlier this year of NAFCU members found that nearly one-in-four have a hard time advertising online or on mobile devices because of these rules. We believe these rules should be amended with the use of social media and mobile banking in mind to include more flexibility as opposed to the rigidity of the current rules. Credit unions have fared very well in safely adopting the use of such technology, and they take actions necessary to ensure their policies and procedures provide oversight and controls with regard to the risk associated by social media activities. A modernization of these rules by NCUA would clear up ambiguity and help credit unions use new technologies to better meet the needs of their members.

Examination Issues

While I have already outlined our support for the Financial Institutions Examination Fairness and Reform Act that was introduced in the last Congress, NAFCU believes that NCUA could take action now to vastly improve the examination process for credit unions.

NAFCU supports effective exams that are focused on safety and soundness and flow out of clear regulatory directives. However, the examination process, by its very nature, can be inconsistent. Regulatory agencies in Washington try to interpret the will of Congress, examiners in the field try to interpret the will of their agency, and financial institutions often become caught in the middle as they try to interpret all three as they run their institution. Unfortunately, the messages are not always consistent.

Exam Modernization

As part of its Regulatory Modernization Initiative, NCUA recently issued its Letter to Credit Unions (Letter No. *13–CU–09*). It streamlined the examination report and clarifies for credit unions the difference between a Document of Resolution (DOR) and an Examiner's Findings Report. Full implementation of these new documents began with exams that started on or after January 1, 2014.

NAFCU has concerns about the continued use of Documents of Resolution (DOR) when they are not necessary or are used in place of open and honest conversations about examiner concerns. Examiner Findings Reports should be used in place of DORs for less urgent issues. That would allow management may use its own discre-

tion to determine the timeframe and approach for correcting those less urgent problems.

Finally, NAFCU believes NCUA should update its exam manual and provide credit unions with the updates so that they may better understand the examination process.

Consistency

One of the most troublesome complaints we hear is that NCUA examinations continue to apply regulations inconsistently. While we fully recognize that examiners must have a certain degree of discretion, as we have previously communicated to the agency, inconsistent examinations and application of regulations create unnecessary confusion and are costly.

Additionally, regulators should ensure that their regulations are consistently applied from one examiner to another. Inconsistent application of laws and regulations among examiners increases uncertainty. This increased uncertainty adds another unnecessary layer of difficulty for credit unions to maintain the highest levels of compliance.

More importantly, it is also unclear how an examiner will evaluate compliance. In addition to actual regulations, NCUA also routinely provides "guidance" in any one of a number of different forms. Some examiners treat the guidance as just that; a tool to be used for credit unions to comply with regulations or implement best practices. Some examiners, however, treat the "guidance" as if it were part of the regulation itself, and consider failure to comply with the guidance as something roughly equal to failing to comply with the regulation. More should be done to ensure that all examiners treat both regulations and guidance consistently and for the purpose each was issued.

Unfortunately, if examinations are not conducted consistently, compliance with the ever-growing number of regulations will be ever more difficult. As a significant percent of examiners are new and with a large number retiring, NCUA will no doubt be continuing to hire new examiners. Thus, we believe that this is a critical juncture, as well as a great opportunity, for the agency to appropriately train and educate examiners so that examinations are conducted consistently. With this goal in mind, NCUA should take any and all measures it deems appropriate to achieve this goal.

Examination Appeal Process

NAFCU understands that some of our concerns cannot be addressed by regulators. Generally, NCUA and its examiners do a satisfactory job, but every inconsistency that forces credit unions to divert more resources to compliance reduces their ability to better serve their members. This ultimately translates to lower interest rates on savings, higher interest rates on loans, and in some cases, the inability to extend credit to a member that would receive credit otherwise.

NAFCU urges reforms to establish an appeals process that should provide an opportunity to identify inconsistencies and serve as a quality assurance check. The existing appeal process does not promote either. Under the existing process, if an examiner makes a determination to take action against the credit union, the credit union must first address the issues with the examiner. The second step is to contact the supervisory examiner, who evaluates the facts and reviews the analysis. If the issue is still not resolved, the credit union may send a letter to the regional director. After the previous steps have been taken, a credit union may then appeal to the NCUA Board for review of the decisions below.

The appeal process has a number of inherent flaws, not the least of which is the exclusion (in most instances) of a review by an independent third-party at any level of the process. Under these circumstances it is almost impossible to avoid conflicts of interest and approach each situation objectively.

CFPB

We would also like to acknowledge efforts by the CFPB to provide relief, such as seeking to act on the privacy notice issue in the absence of any final congressional action and efforts to revisit some of the concerns raised about points and fees under the new QM rule. While we believe that legislative action is still necessary in both regards, the Bureau deserves credit for taking steps in the absence of Congressional action. Still, NAFCU has consistently maintained that the tidal wave of the Bureau's new regulations, taken individually, and more so in their cumulative effect, have significantly altered the lending market in unintended ways. In particular, the ability-to-repay, qualified mortgage, and mortgage servicing rules have required credit unions of various sizes and complexities to make major investments, and incur significant expenses. Taken all together, these regulations have made credit

unions rework nearly every aspect of their mortgage origination and servicing operations.

Exemption Authority

One area where the CFPB could be the most helpful to credit unions would be to use its legal authority to exempt credit unions from various rulemakings. Given the unique member-owner nature of credit unions and the fact that credit unions did not participate in many of the questionable practices that led to the financial crisis and the creation of the CFPB, subjecting credit unions to rules aimed at large bad actors only hampers their ability to serve their members. While the rules of the CFPB may be well-intentioned, many credit unions do not have the economies of scale that large for-profit institutions have and may opt to end a product line or service rather than face the hurdles of complying with new regulation. While the CFPB has taken steps, such as their small creditor exemption, more needs to be done to exempt all credit unions.

Credit unions are also further hampered by the fact that the CFPB does not have one consistent definition of "small entities" from rule to rule. We are pleased that the CFPB makes an effort to meet its obligations under the Small Business Regulatory Enforcement Fairness Act (SBREFA). However, we believe that the Bureau must do more to address the concerns of smaller financial institutions in its final rulemaking, so that new rules do not unduly burden credit unions.

Under SBREFA, the CFPB is required to consider three specific factors during the rulemaking process. First, the agency is to consider "any projected increase in the cost of credit for small entities." Second, the CFPB is required to examine "significant alternatives to the proposed rule which accomplish the stated objective of applicable statutes and which minimize any increase in the cost of credit for small entities." Third, the CFPB is to consider the "advice and recommendations" from small entities. 5 U.S.C. § 603(d). This directive serves an important function. When Congress passed the Dodd-Frank Act, it expected the newly established CFPB to be a proactive regulatory body. NAFCU believes the decision to subject the CFPB to SBREFA was a conscious decision to help ensure that regulations, promulgated with large entities in mind, do not disproportionately impact small financial institutions that were not responsible for the financial crisis.

Regulation E

As NAFCU outlined in our "Top Ten" list of regulations to eliminate or amend in order to better serve credit union customers, the requirement to disclose account numbers on periodic statements should be amended in order to protect the privacy and security of consumers. Under Regulation E, credit unions are currently required to list a member's full account number on every periodic statement sent to the member for their share accounts. Placing both the consumer's full name and full account number on the same document puts a consumer at great risk for possible fraud or identity theft.

NAFCU has encouraged the CFPB to amend Regulation E § 205.9(b)(2) to allow financial institutions to truncate account numbers on periodic statements. This modification is consistent with 12 C.F.R. § 205.9(a)(4), which allows for truncated account numbers to be used on a receipt for an electronic fund transfer at an electronic terminal. This change is also consistent with § 605(g) of the Fair Credit Reporting Act that states, "no person that accepts credit cards or debit cards for the transaction of business shall print more than the last 5 digits of the card number or the expiration date upon any receipt." NAFCU believes that by adopting this change, the CFPB will allow financial institutions to better protect the security and confidentiality of consumer information.

Compromised accounts are not only dangerous for consumers, but can be extremely costly for credit unions. In the past year alone data breaches have cost the credit union industry millions of dollars. According to feedback from our member credit unions, in 2013 each credit union on average experienced $152,000 in loses related to data breaches. The majority of these costs were related to fraud losses, investigations, reissuing cards, and monitoring member accounts. As the recent high-profile data breaches at some of our Nation's largest retailers have highlighted, criminals are willing to go to great extremes to obtain consumer's sensitive financial information. Credit unions understand the importance of steadfastly protecting their member's confidential account information, which is why we strongly suggest this regulatory update.

Until Congress passes new legislation to ensure other third parties, such as merchants, who have access to consumer's financial information, have effective safeguards in place to protect consumer information, the CFPB should consider this minor modification to Regulation E. This change would go a long way in keeping

sensitive financial information out of the hands of criminals and reduce the increasing fraud costs borne by credit unions and other financial institutions.

Remittances

The Dodd-Frank Act added new requirements involving remittance transfers under the Electronic Fund Transfer Act (EFTA) and directed the CFPB to issue final rules amending Regulation E to reflect these additions. Under this mandate, the Bureau, released a series of final rules concerning remittances, all of which became effective on October 28, 2013.

In February 2012, the CFPB issued its first set of final rules on remittances. These rules required, among other things, remittance service providers, including credit unions, to provide a pre-payment disclosure to a sender containing detailed information about the transfer requested by the sender, and a written receipt on completion of the payment. Following the release of the February 2012, final rule, the CFPB issued on August 20, 2012, a supplemental final that provided a safe harbor for determining whether a credit union is subject to the remittance transfer regulations. Specifically, a credit union that conducts 100 or fewer remittances in the previous and current calendar years would not be subject to the rules.

In May 2013, the Bureau modified the final rules previously issued in 2012, to address substantive issues on international remittance transfers. This final rule eliminated the requirement to disclose certain third-party fees and taxes not imposed by the remittance transfer provider and established new disclaimers related to the fees and taxes for which the servicer was no longer required to disclose. Under the rule, providers may choose, however, to provide an estimate of the fees and taxes they no longer must disclose. In addition, the rule created two new exceptions to the definition of error: situations in which the amount disclosed differs from the amount received due to imposition of certain taxes and fees, and situations in which the sender provided the provider with incorrect or incomplete information.

NAFCU opposed the transaction size-based threshold for the final rule's safe harbor. The CFPB relied on an institution size-based threshold, rather than a transaction size-based threshold, in its recently released mortgage rules, and NAFCU urged the Bureau to adopt a similar approach for differentiating between remittance transfer providers. Additionally, NAFCU raised concerns with the final rule's requirement of immediate compliance if an entity exceeds the safe harbor's 100 transaction threshold. It encouraged the CFPB to allow entities who exceed the safe harbor threshold a realistic period in which to meet the standards of the final rule.

NAFCU continues to raise concerns that the regulatory burden imposed by the final rule leads to a significant reduction in consumers' access to remittance transfer services. NAFCU has heard from a number of its members that, because of the final rule's enormous compliance burden, they have been forced to discontinue, or will be forced to discontinue, their remittance programs. A 2013, NAFCU survey of our members found that over one-quarter of those that offered remittance services before the rule have now stopped offering that service to members and even more are considering dropping. Those that continue to offer remittances have been forced to significantly increase their members' fees. NAFCU encourages the CFPB to expand the threshold for the safe harbor from the definition of "remittance transfer provider" in order to ensure that a meaningful safe harbor is established.

HMDA Changes Going Beyond the Dodd-Frank Act

The Dodd-Frank Act transferred Home Mortgage Disclosure Act (HMDA) rulemaking authority to the CFPB and directed the Bureau to expand the HMDA dataset to include additional loan information that would help in spotting troublesome trends. Specifically, Dodd-Frank requires the Bureau to update HMDA regulations by having lenders report the length of the loan, total points and fees, the length of any teaser or introductory interest rates, and the applicant or borrower's age and credit score. However, in its proposal, the Bureau is also contemplating adding additional items of information to the HMDA dataset. NAFCU has urged the CFPB to limit the changes to the HMDA dataset to those mandated by Dodd-Frank.

HMDA was originally intended to ensure mortgage originators did not "redline" to avoid lending in certain geographical areas. The HMDA dataset should be used to collect and provide reasonable data for a specific reason. The Bureau contends that it is going beyond Dodd-Frank's mandated changes to get "new information that could alert regulators to potential problems in the marketplace" and "give regulators a better view of developments in all segments of the housing market." These open-ended statements could be applied to virtually any type of data collection, and do not further the original intent of HMDA. NAFCU urged the CFPB to amend the dataset to advance the original purpose of HMDA, rather than using it as a vehicle to "police" its recent Qualified Mortgage rules.

The various mortgage-related regulations promulgated by the CFPB have exponentially increased credit unions' regulatory burden and compliance costs. Any additions to the HMDA dataset will create even more operational expenses for credit unions. Credit unions that collect and report HMDA data through an automated system will have to work with their staffs and vendors to update their processes and software. Those without automated systems will experience particularly significant implementation costs. The CFPB should eliminate unnecessary regulatory burden and compliance costs by limiting the changes to the HMDA dataset to those mandated by Dodd-Frank.

TILA/RESPA

Dodd-Frank directed the CFPB to combine the mortgage disclosures under the Truth in Lending Act and Real Estate Settlement Procedures Act. Under this mandate, the Bureau, in November 2013, released the integrated disclosures rule. This 1900-page rule requires a complete overhaul of the systems, disclosures, and processes currently in place for a consumer to obtain a mortgage. For example, the rule mandates the use of two disclosures: the three-page Loan Estimate (which replaces the Good Faith Estimate and initial Truth in Lending Disclosure); and the five-page Closing Disclosure (which replaces the HUD–1 and final Truth in Lending disclosure). There are also a number of stringent timing requirements and other substantive changes lenders must follow. The rule is effective August 2015, but lenders are still feeling pressure to be compliant on time. The sheer magnitude of this rule, read in conjunction with the totality of the other mortgage rules, has created a very burdensome regulatory environment and many credit unions are finding it difficult to continue lending. Credit unions must comply with the current disclosure requirements, which are extensive, and they must prepare their compliance solutions for the upcoming ones effective in August 2015, further exacerbating costs.

Qualified Mortgages

NAFCU continues to have serious concerns about the "Qualified Mortgage" (QM) standard. In short, given the unique member-relationship credit unions have, many make good loans that work for their members that don't fit into all of the parameters of the QM box and fall into the "nonqualified mortgage" category. NAFCU would support the changes below to the QM standard to make it more consistent with the quality loans credit unions are already making. Further, credit unions should have the freedom to decide whether to make loans within or outside of the standard without pressure from regulators.

Points and Fees

NAFCU strongly supports bipartisan legislation to alter the definition of "points and fees" under the "ability-to-repay" rule. NAFCU has taken advantage of every opportunity available to educate and discuss with the CFPB on aspects of the ability-to-repay rule that are likely to be problematic for credit unions and their members. While credit unions understand the intention of the rule and importance of hindering unscrupulous mortgage lenders from entering the marketplace, it is time for Congress to address unfair and unnecessarily restrictive aspects of this CFPB rule.

NAFCU supports exempting from the QM cap on points and fees: (1) affiliated title charges, (2) double counting of loan officer compensation, (3) escrow charges for taxes and insurance, (4) lender-paid compensation to a correspondent bank, credit union or mortgage brokerage firm, and (5) loan level price adjustments which is an upfront fee that the Enterprises charge to offset loan-specific risk factors such as a borrower's credit score and the loan-to-value ratio.

Making important exclusions from the cap on points and fees will go a long way toward ensuring many affiliated loans, particularly those made to low- and moderate-income borrowers, attain QM status and therefore are still made in the future.

Loans Held in Portfolio

NAFCU supports exempting mortgage loans held in portfolio from the QM definition as the lender, via its balance sheet, already assumes risk associated with the borrower's ability-to-repay.

40-year Loan Product

Credit unions offer the 40-year product their members often demand. To ensure that consumers can access a variety of mortgage products, NAFCU supports mortgages of duration of 40 years or less being considered a QM.

Debt-to-Income Ratio

NAFCU supports Congress directing the CFPB to revise aspects of the 'ability-to-repay' rule that dictates a consumer have a total debt-to-income (DTI) ratio that is less than or equal to 43 percent in order for that loan to be considered a QM. This arbitrary threshold will prevent otherwise healthy borrowers from obtaining mortgage loans and will have a particularly serious impact in rural and underserved areas where consumers have a limited number of options. The CFPB should either remove or increase the DTI requirement on QMs.

Legal Opinion Letters

In attempting to understand ambiguous sections of CFPB rules, NAFCU and many of its members have reached out to the CFPB to obtain legal opinion letters as to the agencies interpretation if it's regulations. While legal opinion letters don't carry the weight of law, they do provide guidance on ambiguous section of regulations. Many other financial agencies such as NCUA, FTC, FDIC and others issue legal opinion letters so as to help institutions and other agencies understand otherwise ambiguously written rules. The CFPB has declined to do so. What they have done is set up a help line where financial institutions can call for guidance from the agency. While this is helpful, there are reports of conflicting guidance being given depending on who answers the phone. This is not just unhelpful, but confusing when NCUA examines credit unions for compliance with CFPB regulations.

Federal Reserve Board

NAFCU has long encouraged the Federal Reserve to update Regulation D. This issue is also on NAFCU's "Dirty Dozen" and "Top Ten" list. Regulation D generally imposes reserve requirements on depository institutions with transaction accounts or nonpersonal time deposits, and requires reporting to the Federal Reserve. The regulation aims to facilitate monetary policy and ensure sufficient liquidity in the financial system. It requires credit unions to reserve against transaction accounts, but not against savings accounts and time deposits.

NAFCU believes the Federal Reserve Board should revisit the transaction limitation requirements for savings deposits. The six-transaction limit imposes a significant burden on both credit union members in attempting to access and manage their deposits and credit unions in monitoring such activity. Member use of electronic methods to remotely access, review and manage their accounts, as well as the contemporary transfer needs of members and consumers at all types of financial institutions, make a monthly transaction limit an obsolete and archaic measure. Should the Board decide not to outright remove the transaction limitation requirement for savings deposits, NAFCU has urged the Board to raise the current limitation from six to 12 transactions. If the Board fails to act in this area, we believe Congress should be ready to address this issue. We were pleased to see House Financial Services Committee Chairman Jeb Hensarling and Representative Robert Pittenger request a GAO study on this issue.

FHFA

In September 2014, FHFA released a proposed rule that would establish new asset threshold for both FHLB applications and ongoing membership. Specifically, FHLB members and applicants would be required to keep 1 percent of assets in home mortgage loans. Also, current FHLB members would be required to hold at least 10 percent of assets in residential mortgage loans on an ongoing basis—a marked change from the current rule, which only requires this 10 percent threshold at the application stage. The proposal would also require FHLBs to evaluate member compliance annually and to terminate membership after two consecutive years of noncompliance. This proposed rule threatens to severely hamper credit unions' access to the valuable services the FHLBs provide and must be carefully considered for its full impact before moving forward. In 2007, 11.4 percent of credit unions were members of an FHLB, representing 61.7 percent of total credit union assets. Today, however, 19 percent of all credit unions are members of an FHLB, and these credit unions represent 75.8 percent of the total credit union assets and this number continues to grow. This growth of credit union membership in FHLBs only underscores the need to ensure that the eligibility requirements for membership in FHLBs are set appropriately. Unfortunately, this proposal would disenfranchise over 1 million credit union member-owners from receiving the benefits of FHLB resources as their institution's membership would be terminated under the newly proposed requirements.

While NAFCU appreciates FHFA's intention of fostering FHLB's housing finance missions, we believe the current regulatory requirements effectively ensure that FHLB members demonstrate ongoing commitments to mortgage lending in their

communities. For example, when an FHLB member borrows an advance, it must provide eligible collateral to secure the advance. Nearly all eligible types of collateral, which are determined by Congress, are related to housing. In addition, current members must certify their active support of housing for first-time home buyers to the FHFA every 2 years through the Community Support Statement. Further, FHFA has failed to provide any data or empirical evidence to support its claims that the FHLB system is at risk because some members may not meet the proposed asset percentage requirements on an ongoing basis. Given the sufficient existing requirements, and the lack of statistical support for the proposed changes, NAFCU does not believe FHFA needs to move forward with the newly proposed "ongoing" membership requirements for depository institutions in this rulemaking.

Further exacerbating this issue for credit unions is the statutory exemption for FDIC-insured banks with under $1.1 billion in assets from the 10 percent requirement as outlined in the Federal Home Loan Bank Act. In addition to seeking changes to the underlying FHFA proposal, NAFCU believes this discrepancy also needs to be addressed to ensure an even playing field between all financial institutions including credit unions on this matter. We would urge the committee to act on this matter and create parity for credit unions.

IX. Department of Defense (Military Lending Act Proposed Rule)

NAFCU is in full support of protecting servicemembers from predatory and unscrupulous lenders. It is clear this is the intent of the proposed rule DoD has issued. Unfortunately, and unlike the original regulation promulgated by DoD in 2007, this rule does not take into account the unintended consequences to the financial industry. While well-intentioned, the rule creates a significant and unnecessary regulatory burden on financial institutions particularly for small community institutions like credit unions.

The burden is significant because it will force all lenders to add an extra time consuming and costly step to essentially every extension of consumer credit. Under the DoD proposed rule, all lenders would be forced to determine if any individual receiving consumer credit is a servicemember or a dependent of a servicemember. While the rule provides flexibility in the manner in which a lender could determine the status of a borrower, it only grants a safe harbor from civil and potentially criminal penalties if the lender uses the Defense Manpower Data Center (DMDC) database. Additionally, even this safe harbor can become invalid if it is found that financial institution had actual knowledge of a borrower's status.

This presents a number of issues for credit unions particularly small credit unions. First, every lender would be forced to review all information and documentation on every existing member or customer to determine if they have actual knowledge of the status of that particular individual. This would produce a significant cost to a lender to not only review all records but also to implement a system of checks to ensure that any information given to them in the future that could serve as actual knowledge is documented.

Second, lenders would have to institute a set of procedures to check the DMDC database for every extension of consumer credit. Credit unions would either have to manually check the database in every situation or pay what could amount to an enormous cost to integrate an automated system into their current systems. This burden would be created for virtually every extension of credit to identify individuals that may makeup less than 1 percent of a credit union's membership.

As noted, NAFCU supports providing servicemembers with protections, and if incurring the unintended consequences of this rule was the only way to protect service members, this would certainly be a different discussion. What is most perplexing about the DoD rule is the fact that there is a very simple solution to this problem that would significantly reduce the burden on credit unions and lenders while still providing servicemembers with the same protections. This solution is self-identification. If service members self-identify themselves, virtually all the unnecessary burden of the rule would be mitigated and service members would still receive the protections intended by the rule. This method has worked extremely well with the interest rate reduction required under the Servicemembers Civil Relief Act (SCRA).

Another major concern regarding the rulemaking has been the process. While this rule will effectively cover almost every lender in the Nation, the Department of Defense has refused to meet with industry to discuss how this rule could be implemented in the most effective manner. Given the opportunity, we believe that industry could make a valuable contribution to ensuring this rule works both effectively and efficiently.

X. Regulatory Coordination is also Needed

With numerous new rulemakings coming from regulators, coordination between the agencies is more important than ever. Congress should use its oversight authority to make sure that regulators are coordinating their efforts and not duplicating burdens on credit unions by working independently on changes to regulations that impact the same areas of service. There are a number of areas where opportunities for coordination exist and can be beneficial. We outline two of them below.

Financial Stability Oversight Council (FSOC)

NAFCU has been on the forefront encouraging the FSOC regulators to fulfill their Dodd-Frank mandated duty to facilitate rule coordination. This duty includes facilitating information sharing and coordination among the member agencies of domestic financial services policy development, rulemaking, examinations, reporting requirements and enforcement actions. Through this role, the FSOC is effectively charged with ameliorating weaknesses within the regulatory structure and promoting a safer and more stable system. It is extremely important to credit unions for our industry's copious regulators to coordinate with each other to help mitigate regulatory burden. We urge Congress to exercise oversight in this regard and consider putting into statute parameters that would encourage the FSOC to fulfill this duty in a thorough and timely manner.

Data Security

Outside of advocating for Federal legislation with regard to the safekeeping of information and breach notification requirements for our Nation's retailers, NAFCU has also urged regulatory coordination for credit unions already in compliance with the stringent standards in the *Gramm-Leach-Bliley Act.* In the wake of the massive Target data breach in December 2013 the Federal Trade Commission began exploring a range of regulatory options to assist consumers, businesses, and financial institutions. Moving forward, it is imperative that NCUA ensure that credit unions are protected from any unnecessary regulatory burden and continue to allow them to provide quality services to their members.

Congress must also act to establish a national data security standard for retailers who hold personal financial data. The financial services industry has been subject to such a standard since the passage of Gramm-Leach-Bliley in 1999, it's time for others who hold financial data are held to a similar standard. While it is not the subject of this hearing, we hope that the Committee will make addressing data security concerns one of its priorities in the 114th Congress.

XI. Conclusion: All Credit Unions Need Regulatory Relief

The growing regulatory burden on credit unions is the top challenge facing the industry today and credit unions are saying "enough is enough" when it comes to the over regulation of the industry. All credit unions are being impacted regardless of asset size. This burden has been especially damaging to smaller institutions that are disappearing at an alarming rate. The number of credit unions continues to decline, as the compliance requirements in a post Dodd-Frank environment have grown to a tipping point where it is hard for many smaller institutions to survive. Those that do are forced to cut back their service to members due to increased compliance costs.

Credit unions want to continue to aid in the economic recovery, but are being stymied by this over regulation. NAFCU appreciates the Committee holding this hearing today. Moving forward, we would urge the Committee to act on credit union relief measures pending before the Senate and the additional issues outlined in NAFCU's Five Point Plan for Credit Union Regulatory Relief and NAFCU's "Top Ten" list of regulations to review and amend. Additionally, Congress needs to provide vigorous oversight to the NCUA's proposed risk-based capital rule and be ready to step in and stop the process so that the impacts can be studied further. Finally, the Committee should also encourage regulators to act to provide relief where they can without additional congressional action.

We thank you for the opportunity to share our thoughts with you today. I welcome any questions you might have.

PREPARED STATEMENT OF MICHAEL D. CALHOUN

PRESIDENT, CENTER FOR RESPONSIBLE LENDING

FEBRUARY 12, 2015

Good morning Chairman Shelby, Ranking Member Brown, and Members of the Senate Committee on Banking, Housing, and Urban Affairs. Thank you for allowing

me the opportunity to testify on regulatory relief for community banks and credit unions and the need to ensure that all financial institutions, regardless of their size, are subjected to responsible regulatory oversight that maintains consumer financial protections.

I am the President of the Center for Responsible Lending (CRL), a nonprofit, nonpartisan research and policy organization dedicated to protecting homeownership and family wealth by working to eliminate abusive financial practices. CRL is an affiliate of Self-Help, a nonprofit community development financial institution. For 30 years, Self-Help has focused on creating asset building opportunities for low-income, rural, women-headed, and minority families. In total, Self-Help has provided $6 billion in financing to 70,000 home buyers, small businesses, and nonprofits and currently serves more than 80,000 mostly low-income families through 30 retail credit union branches in North Carolina, California, and Illinois. As the General Counsel of Self-Help for 20 years, I can personally attest to the fact that responsible regulations and regulatory oversight are critical to the success of a small lender.

I. Differences Exist for Community Banks and Credit Unions.

Community lenders and credit unions, and the financial services they provide, are both important and distinctive. We appreciate that small lenders and credit unions frequently use a different business model to provide financial services to consumers, one that usually involves smaller transactions and is based on the institution having much closer ties to both the borrowers and communities that they serve. The result is a tailored lending and underwriting process that can produce more successful lending. Also, unlike their larger bank counterparts, smaller financial institutions are less likely to participate in capital market transactions. Previous testimony from industry organizations, like the American Bankers Association and the Independent Community Bankers of America, has shown that community banks oversee a much smaller percentage of the Nation's financial assets—on average less than $1 billion at each institution—and operate with far fewer employees, with industry estimates ranging from staff averages of 40 to 54.[1]

Given the differences in business practices, business scale, and company resources, CRL supports a regulatory framework and oversight structure that appropriately recognizes and accommodates the unique nature of community banks and credit unions. It is important that regulators understand how small lending institutions work and take those factors into account when regulating. One-size regulation does not always fit all. Community banks and credit unions must be able to continue successfully conducting business in America's communities.

II. Financial Regulations are Important.

Yet, it is important to remember why regulations, especially financial regulations, are essential to preserving the financial health of American consumers and the health of this Nation's economy. Responsible financial regulations protect consumers from abusive and harmful financial products, ensure the safety and soundness of financial institutions, and prevent systemic risk from threatening to undermine the Nation's financial market as a whole.

Recent history has already shown us the consequences of under-regulation in the financial market. In the wake of the financial crisis, 5.5 million American consumers have lost their homes through foreclosure.[2] And, according to the Federal Deposit Insurance Corporation, more than 500 banks shuttered their doors; most of those institutions were community banks.[3] The failure to have a responsible regulatory environment also resulted in taxpayers paying $7 trillion to bail out financial institutions through loans and, according to some reports, an additional $22 trillion through the Federal Government's purchase of assets.[4] In addition, the national economy was undermined and plunged into a severe recession. People lost their jobs, small businesses went under, and many Americans—from small entrepreneurs to families-struggled to make ends meet while being unable to obtain the credit and

---

[1] Jeff Plagge, American Bankers Association, Hearing before the Senate Committee on Banking, Housing, and Urban Affairs, *Examining the State of Small Depository Institutions,* 113th Cong. 2d sess, 2014; John Buhrmaster, Independent Community Bankers of America, Hearing before the Senate Committee on Banking, Housing, and Urban Affairs, *Examining the State of Small Depository Institutions,* 113th Cong. 2d sess, 2014.

[2] Corelogic, "CoreLogic Reports 41,000 Completed Foreclosures in November 2014," (January 14, 2015) *accessed at http://investor.corelogic.com/mobile.view?c=118425&v=203&d=1&id=2007499.*

[3] Federal Deposit Insurance Corporation, *Failed Bank List, accessed at https://www.fdic.gov/bank/individual/failed/banklist.html.*

[4] John Carney, "The Size of the Bank Bailout: $29 Trillion," *CNBC,* December 14, 2011, *accessed at http://www.cnbc.com/id/45674390#.*

capital they needed from financial institutions in order to sustain their position or expand their asset base.

The negative nature of these consequences make it clear to CRL that proactive, responsible financial regulations—like those being enacted under the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank)[5]—are needed to protect consumers, small businesses, taxpayers, and the Nation's economy. And it is equally clear that oversight is necessary for every actor in the financial market, whether they are as large as J.P. Morgan Chase, a mid-size institution like Synovus, community bank lenders like Georgia Bank & Trust and First National Bank of Scotia, or credit unions like SRP Federal Credit Union and CRL's affiliate, Self-Help. All financial institutions, including community banks and credit unions, benefit from the underlying purposes of financial regulation: protecting consumers, ensuring the safety and soundness of institutions, protecting community financial institutions from unfair competition, and defending the Nation's financial market from systemic risk. The question is whether there are different, more efficient ways to effectively ensure that these objectives are being met when regulating community banks and credit unions.

III. Relief for Community Financial Institutions Should Be Targeted to Those Institutions.

During the 113th Congress, a number of bills and other industry proposals were introduced under the banner of providing regulatory relief to community banks that, in reality, would have primarily or solely benefited regional, mid-size institutions. These bills and proposals included provisions to:

- Amend the Consumer Financial Protection Act, a component of Dodd-Frank, to raise the examination threshold that brings an insured depository institution or insured credit union within CFPB's supervisory purview from assets of $10 billion or more to assets of $50 billion or more;[6]
- Increase the threshold size of an insured depository institution or insured credit union that is subject to the Consumer Financial Protection Act's reporting requirements from assets of $10 billion or more to $50 billion or more;[7]
- Exempt creditors with under $50 billion in assets from the escrow account requirement for first lien, higher-priced mortgages held in portfolio as required by the Dodd-Frank Act; and[8]
- Exempt institutions with less than $50 billion in assets from the Volcker Rule's compliance requirements if they are not involved in any activities under the law and even remove their obligation to analyze their trading and investments to ensure that their activity is exempt.[9]

The reality is that, in terms of asset size, geographic base, and company resources, institutions with assets between $10 to $50 billion look very different than a traditional community bank. CRL's analysis shows that while community banks have on average less than 54 employees, the institutions that stand to benefit from these proposals have an average of more than 2,500 employees. Compliance costs related to staffing resources can hardly be viewed as parallel.

Moreover, while the business model of community banking is predicated on strong community relationships in a concentrated geographic market, many of the institutions that stand to benefit from these provisions have nationwide markets. These institutions are large players with familiar names, like Morgan Stanley Private Bank, American Express Bank, GE Capital Bank, and E*Trade Bank. Many people would be surprised to hear these institutions called community banks. They would also be surprised to learn that American Express Bank is considered as somehow having the same business model and compliance cost challenges as First National Bank of Scotia, an institution with 10 banking branches located in a single State and operating with fewer than 200 employees.

Asset size alone may not accurately define a community bank. Yet, organizations as diverse as the FDIC,[10] American Enterprise Institute,[11] and CRL agree that a

[5] Public Law 111–203 (2010).
[6] Consumer Financial Protection Bureau Examination and Reporting Threshold Act of 2014, S. 2732, 113th Cong. (2014).
[7] Consumer Financial Protection Bureau Examination and Reporting Threshold Act of 2014, S. 2732, 113th Cong. (2014).
[8] Community Lending Enhancement and Regulatory Relief Act of 2013, H.R. 1750, 113th Cong. (2014).
[9] Independent Community Bankers of America, *ICBA Policy Resolutions for 2014.*
[10] Federal Deposit Insurance Corporation, *Community Banking Study.*
[11] American Enterprise Institute, *The Impact of Dodd-Frank on Community Banks.*

business model focused on relationship-based lending, geographically concentrated business market, and limited business resources are important supplementing factors that complete the definition. The FDIC's recently updated analysis of its 2012 Community Banking Study notes that, using these factors, 94 percent of all community banks have assets under $10 billion and 90 percent of those institutions have assets under $1 billion.[12] Moreover, 80 percent of credit unions have less than $100 million in assets.[13] Therefore, so-called community bank provisions that provide exemptions for the 72 institutions holding between $10 to $50 billion in assets do little to help the more than 6,000 community banks that provide credit and capital across this country.

IV. Substantive Rollbacks of Dodd-Frank are not Community Bank Regulatory Relief.

A number of community bank regulatory relief proposals focus on making substantive changes to the mortgage protections put in place by Dodd-Frank. For example, proposals like those to remove the escrow requirement for institutions with less than $50 billion in assets threaten to erase important consumer protections for millions.[14] Under the CFPB's implemented regulations for Dodd-Frank, escrows are required only on higher priced mortgages-and even this requirement only applies for the first years of the loan to ensure that the loan is sustainable. Escrow accounts protect consumers by ensuring that they have funds for reoccurring homeownership-related expenses, such as property taxes and insurance premiums, thereby reducing the likelihood of default.

Another proposal, to exclude appraisal requirements for loans under $250,000 is so broad in scope that it would allow nondepository lenders to benefit along with all banks and credit unions.[15] These very nonbank lenders were key players in the financial crisis and are already subject to less oversight because of their nondepository status. The appraisal exemption for $250,000 loans is also overly broad because it would apply to nearly half of all homes in the United States. In 2014, the median sales price for existing homes in the United States was only $209,500. It is important for everyone to remember that mortgage appraisal fraud was a key driver of the housing bubble and subsequent bust.[16]

Nearly 9 out of 10 mortgages in the United States are made by noncommunity bank lenders.[17] Substantive rollbacks of Dodd-Frank's mortgage provisions with broad applicability undermine Dodd-Frank's goal of protecting consumers as a whole and preventing the recurrence of another foreclosure crisis. Rollbacks should not be included in community bank regulatory relief legislation.

V. Regulators are moving in the right direction by making efforts to reduce regulatory burdens for small lenders.

The focus should be on what will help traditional community banks and credit unions, while protecting consumers, the institutions, and the Nation's economy as a whole. Thankfully, the Consumer Financial Protection Bureau, Office of the Comptroller of the Currency, Federal Deposit Insurance Corporation, and National Credit Union Administration have been mindful of the differences between larger institutions and smaller lenders and are working to tailor rules implementing Dodd-Frank accordingly.

The CFPB, in particular, has developed a successful track record in taking the lead to adopt and consider regulations that are balanced for financial institutions and accommodate smaller lenders. For example, the CFPB recently requested comment on whether to increase the 500 first-lien mortgage cap under QM's small-creditor definition. CRL expressed support for a reasonable increase of the 500 loan cap, limiting any potential increase to rural banks or for loans held in portfolio. The CFPB's proposal quadruples the limit, expanding the loan origination cap for small lenders from 500 first-lien mortgages to 2,000. This 2,000 limit is exclusive of loans held in portfolio by both the creditor and its affiliates.

The CFPB has also proposed to only include first-lien mortgage originations of small lender affiliate assets toward the current $2 billion small lender asset cap.

[12] Federal Deposit Insurance Corporation, *FDIC Quarterly 2014, Volume 8, Number 2.*

[13] Larry Fazio, National Credit Union Administration, Hearing before the Senate Committee on Banking, Housing, and Urban Affairs, *Examining the State of Small Depository Institutions,* 113th Cong. 2d sess, 2014.

[14] Community Lending Enhancement and Regulatory Relief Act of 2013, H.R. 1750, 113th Cong. (2014).

[15] Community Lending Enhancement and Regulatory Relief Act of 2013, H.R. 1750, 113th Cong. (2014).

[16] Federal Bureau of Investigation, *2010 Mortgage Fraud Report.*

[17] Federal Deposit Insurance Corporation, *Statistics on Depository Institutions.*

And, to accommodate concerns that the definition of a "rural and underserved" area is too narrow, the CFPB has proposed expanding the definition of rural areas by including census blocks as defined by the Census Bureau. Finally, the CFPB is also proposing to allow grace and qualifying periods for small creditors to adjust to current and proposed standards. While we may not always agree on all specifications, we have and continue to support the CFPB's ongoing efforts to reasonably explore how mortgage rules can further accommodate small lenders and lending in designated rural and underserved areas.

In addition to the CFPB's activity with mortgage rules, financial regulators are working with industry, consumer groups, and other stakeholders to review their regulatory framework, as required by the Economic Growth and Regulatory Paperwork Reduction Act of 1996.[18] Under the existing law, the agencies must eliminate any unnecessary regulations and are required to report their actions to Congress next year.

Finally, regulators have reported that technical assistance and ombudsman programs have been extremely effective vehicles for providing regulatory assistance to community banks and credit unions. The effectiveness of these programs, however, depends upon adequate funding. CRL recommends that any regulatory relief legislation include increased funding for regulators' technical assistance and ombudsman activities.

VI. Conclusion

Community banks and credit unions play an important and essential role in this Nation's financial market. Therefore, CRL understands the need for appropriate regulatory flexibility for small depositories. We oppose, however, any effort to use regulatory relief for community banks and credit unions as a vehicle for nondeposit-taking lenders, mid-size and large financial institutions to avoid having the regulatory scrutiny and oversight that proved lacking in the buildup to the financial crisis. The need for regulatory flexibility must be balanced against the importance of consumer safeguards, an institution's safety and soundness, and the security of America's financial system as a whole. Federal financial regulators, like the CFPB, must be allowed to both protect the American people and ensure access to a broad, sustainable financial market.

I look forward to continuing to work with this Committee, community banks and credit unions, their associations, and regulators, to ensure that all of these objectives are satisfied through laws and responsible regulations. Thank you for the opportunity to testify today, and I look forward to answering your questions.

[18] Public Law 104–208 (1996), codified at 12 USC § 3311.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR BROWN FROM WALLY MURRAY

Q.1. At Tuesday's hearing, NCUA stated that its top priority was to obtain authority from Congress to examine third-party vendors. In addition to its arguments that it would reduce burdens for credit unions, it made the case that this authority is vitally important to protect the smallest credit unions from cyber-attacks. What are your views on this proposal?

A.1. We disagree with the assertion that providing NCUA with authority to examine third-party vendors would reduce regulatory burden. Moreover, we disagree with the premise that adding an additional layer of regulation could reduce regulatory burden. NCUA has several tools at its disposal to ensure that credit unions conduct due diligence in establishing and maintaining relationships with credit union service organizations and other third-party vendors. It seems unlikely that NCUA would reduce its expectation on credit unions with respect to due diligence if it had authority to examine third-party vendors and more likely that these vendors would spread the cost of examinations to their credit union customers. Further, NCUA already has the authority to require credit unions to provide information on the credit union service organizations that they own—and, indeed, already requires this through a 2014 regulation. Providing NCUA with additional authority in this area will increase regulatory burden and costs for all credit unions without meaningfully improving the safety and soundness of the credit union system or providing benefit to credit union members.

Likewise, we question NCUA's assertion that increased authority is necessary to protect the smallest credit unions from cyber-attacks. Protecting critical infrastructures from cyber-attacks is a significant national security issue, one on which the Department of Homeland Security and other agencies have the expertise and have taken the lead. Given the coordinated nature of these efforts, we are concerned that providing NCUA with additional authority could be counterproductive given the comparatively light expertise the agency has on these matters.

Q.2. As the Committee considers proposals to provide regulatory relief to community banks and small credit unions, I am reminded of an exchange that I had with then Fed Chairman, Bernanke, in July 2013. At that hearing he indicated that regulators should "do whatever we need to do to make sure the U.S. financial system is safe." Do you agree that this is the regulators' primary objective?

A.2. There is no doubt that safety and soundness has paramount importance—after all, if there is no confidence in the safety of the financial system, it will collapse. Regulators play an important role in this regard, but they are not the only ones capable of managing safety and soundness. Credit unions have demonstrated a strong

historical track record of managing our institutions prudently, through even the most challenging economic times, because we inherently understand that do so is in the best interest of our members.

It is important for the financial system to be regulated in a manner that allows providers to offer products and services to the users at rates and terms that are agreeable. NCUA's mission statement acknowledges this dual responsibility to promote safety and soundness and encourage the availability of credit union services to members: "The mission of the NCUA is to facilitate the availability of credit union services to all eligible consumers, especially those of modest means, through a safe and sound credit union system." (*www.ncua.gov*).

This is why regulatory relief for credit unions is so important. When the regulator errs on the side of too much caution in terms of safety and soundness, the ability of credit unions to serve their members is restricted. We believe there are several areas of regulation and statute that are unnecessary from a safety and soundness perspective and should be altered or removed altogether.

RESPONSE TO WRITTEN QUESTION OF SENATOR COTTON FROM WALLY MURRAY

Q.1. As far as you are aware, to what extent (or lack thereof) has CFPB exercised its exemption authority under Section 1022 of Dodd-Frank? Is this concerning given the broad scope and lengthy detail of some of its rulemakings, which, while not aimed at small financial institutions, can substantially and negatively impact those businesses?

A.1. Although we recognize that the CFPB has exercised its exemption authority in important ways, and has taken positive steps to revisit small institution exemptions in some areas recently, the Bureau can and should do much more.

In many cases, the exemption levels the Bureau has provided are much too low to be useful in the real world. For example, the exemption level for the international remittances rule works out to be approximately two transactions per week. For a product that depends on transaction volume in order to make offering the service economically viable, this is far too low. As a result, many credit unions have stopped providing this important service to their members. There are many other examples of exemption levels set too low, such the small servicer exemption to the mortgage servicing rules.

Regrettably there are several rules for which the Bureau could have provided small institution exemptions but did not, including the HOEPA rules, appraisal rules under Regulation B and Regulation Z, and importantly, the TILA–RESPA rule that becomes effective in August.

Credit unions were not engaging in the risky products and services that caused the financial crisis. They should not be regulated in the same way as those that did. Regulating credit unions in the same way as the largest banks has the net effect of reducing lending, harming credit union members and communities from coast to coast. When a rule intended to reign in large banks or nonbank fi-

nancial service providers results in fewer credit unions providing the service, consumer protection suffers, the large banks just get larger, and the rule has failed.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR BROWN FROM JOHN H. BUHRMASTER

Q.1. At the Banking Committee's February 10, 2015 hearing on regulatory relief, the OCC and FDIC proposed an increase from $500 million to $750 million the asset-size threshold that determines whether a community bank can qualify for an examination every 18 months, rather than every 12 months. What do you think about this proposal?

A.1. ICBA strongly supports the proposal. However, we would like to see the proposal expanded to include banks with assets up to $2 billion and we would like to extend the exam cycle from 18 months to 2 years. Since this provision would only apply to well rated banks, we believe extending the cycle is justifiable and would not impair the ability of regulators to supervise these banks. Even banks on an 18-month cycle, have contact and oversight by their regulators at least quarterly if not more frequently. An extension of the exam cycle would not result in any increase in safety and soundness risk. Quite to the contrary, it would allow us to devote more resources to our operational and lending risk review, and less to exam and compliance risk responses.

Q.2. As the Committee considers proposals to provide regulatory relief to community banks and small credit unions, I am reminded of an exchange that I had with then Fed Chairman, Bernanke, in July 2013. At that hearing he indicated that regulators should "do whatever we need to do to make sure the U.S. financial system is safe." Do you agree that this is the regulators' primary objective?

A.2. Yes, the primary objective of bank regulation should be safety and soundness. However, we believe regulatory burden is threatening the safety and soundness of community banks. Many community banks cannot survive under the current burden and are being forced to merge or consolidate with other banks. For these reasons, ICBA is strongly advocating for its Plan for Prosperity—a set of proposals designed to reduce the onerous burden on community banks and the communities they serve. A good example is at my own bank. We have rated compliance and exam risk to be higher than lending risk, and therefore several years ago reassigned our most skilled commercial lending analyst to compliance. We have a strong and conservative lending history, very similar to most community banks, and yet the regulatory burden has caused us to take our most talented individuals and assign them to compliance, and not to our 91-year-old focus, helping make peoples' lives better.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR VITTER FROM JOHN H. BUHRMASTER

Q.1. Mr. Buhrmaster, as I am sure you are aware the Federal Deposit Insurance Corporation (FDIC) recently released a statement encouraging, "institutions to take a risk-based approach in assessing individual customer relationships rather than declining to pro-

vide banking services to entire categories of customers." This was in response to requests from Congress over concerns of the financial task force known as "Operation Choke Point."

As President of your bank did you ever feel any pressure from any apparatus of the Federal Government not to bank any category of business? Do you believe that this statement by the FDIC will stop Operation Choke Point?

A.1. My bank is nationally chartered and regulated by the OCC and my bank did not feel regulatory pressure aimed at specific business lines. However, as I've talked with bankers nationally, I heard many instances of regulatory overreach targeted at banks providing payment services to payday lenders and money service businesses. The statement by the FDIC represents a step in the right direction, but community banks will not know the impact of the FDIC's recent statement until their next safety and soundness examination. Our examiners have required us to provide risk analysis to our minute ACH origination program that far exceeds our risk with our low volume, and the minimal fees we get for the service. We reexamine the rational for maintaining this business line each year due to these burdensome regulatory requirements.

Q.2. Mr. Buhrmaster, the Nation's largest Wall Street banks enjoy an implicit guarantee—funded by taxpayers and awarded by virtue of their size—as the market knows that these institutions have been deemed "too-big-to-fail. This allows the Nation's largest megabanks to borrow at a lower rate than regional banks, community banks, and credit unions. This funding advantage, which has been confirmed by three independent studies, is estimated to be as high as $83 billion per year.

As Chairman of the Independent Community Bankers of America do you agree that the Nation's largest banks have an unfair advantage over community banks? What steps do you believe need to be taken to fix this inequity?

A.2. We agree that there is an unlevel playing field in banking and that the large, TBTF banks enjoy an unfair funding advantage over community banks. The continued growth and dominance of these banks has created an overly concentrated financial system, created unacceptable moral hazard and systemic risk, thwarted the operation of the free market, and harmed consumers and business borrowers. Although we support some of the enhanced prudential standards that the regulators have been imposed on the large banks such as additional capital and liquidity standards, OLA and contingent resolution plans, we do not believe these steps by themselves will eliminate the TBTF advantage. We believe the only way to truly eliminate the advantage and level the playing field is by restructuring the banking system. ICBA supports FDIC Vice Chairman Tom Hoenig's proposal to restructure banking organizations to prevent extension of the Federal safety net and reduce systemic risk. Under the Hoenig proposal, banks would be restricted to core banking activities and would be prohibited from engaging in risky nonbanking activities.

RESPONSE TO WRITTEN QUESTION OF SENATOR COTTON FROM JOHN H. BUHRMASTER

Q.1. As far as you are aware, to what extent (or lack thereof) has CFPB exercised its exemption authority under Section 1022 of Dodd-Frank? Is this concerning given the broad scope and lengthy detail of some of its rulemakings, which, while not aimed at small financial institutions, can substantially and negatively impact those businesses?

A.1. CFPB has exercised its exemption authority on a number of occasions to provide tiered regulation for small institutions or institutions with a small volume of activity. Examples include: the small creditor portfolio loan exception under the Ability to Repay/Qualified Mortgage rules (banks under $2 billion in assets that originate fewer than 500 first lien mortgages per year; pending proposed would increase the limit to 2,000 loans per year excluding portfolio loans); the small servicer exception under the Mortgage Servicing rule (for those servicing 5,000 loans or fewer); the Escrow rule exception (for small rural creditors); and the Remittances rule exemption (institutions sending fewer than 100 remittances a year).

While these exceptions and exemptions are appreciated, community banks are still overburdened with regulatory requirements that are not necessary to ensure they make high quality, safe loans, or provide fair and transparent services to their customers. In many cases, the exceptions and exemptions should be broader to encompass more community banks. For example, we bump up against the remittance rule of 100 each year, and each year we consider dropping the service. If we go over, we will drop the program, as the risk of the additional compliance will outweigh any potential gain. In any case, the portions of the rules that do apply to community banks comprise hundreds and hundreds of pages of complex and detailed requirements that consume large quantities of time and resources to implement and maintain. In many cases, the requirements make it increasingly difficult for community banks to provide competitive products and services to their customers, thereby reducing access to credit in some communities and eliminating options and choices for consumers who need it most.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR BROWN FROM ED TEMPLETON

Q.1. At Tuesday's hearing, NCUA stated that its top priority was to obtain authority from Congress to examine third-party vendors. In addition to its arguments that it would reduce burdens for credit unions, it made the case that this authority is vitally important to protect the smallest credit unions from cyber-attacks. What are your views on this proposal?

A.1. NAFCU does not support this proposal. We do not believe spending credit union resources to expand NCUA's examination authority into noncredit union third parties is a wise use of resources. While NCUA contends that examination and enforcement authority over third-party vendors will provide regulatory relief for the industry, NAFCU and our members firmly believe that such authority is unnecessary and will require considerable expenditure of the

agency's resources and time. NAFCU disagrees with the assertion that third-party vendor examination and enforcement authority will provide any significant improvement to credit union safety and soundness. While cybersecurity is an extremely important issue, NAFCU does not believe that cybersecurity and third-party vendor authority go hand in hand.

The key to success with appropriate management of vendors is due diligence on behalf of the credit union. NAFCU supports credit unions being able to do this due diligence and NCUA already offers due diligence guidance to credit unions. Given this fact, we believe NCUA already has tools to address any issues through the credit union examination process. NAFCU believes that giving NCUA additional authority is unlikely to provide additional protection to credit unions. This new authority would require an additional outlay of agency resources, which will, in turn, necessitate higher costs to credit unions.

Q.2. As the Committee considers proposals to provide regulatory relief to community banks and small credit unions, I am reminded of an exchange that I had with then Fed Chairman, Bernanke, in July 2013. At that hearing he indicated that regulators should "do whatever we need to do to make sure the U.S. financial system is safe." Do you agree that this is the regulators' primary objective?

A.2. Safety and soundness is a critical responsibility for regulators, but there can be different interpretations on what steps should be taken to achieve it. Ensuring that financial institutions can continue to provide financial services to the American public in the most efficient manner, without compromising safety and soundness, is also critical. The primary objective of a regulator should be to keep an industry safe, while at the same time facilitating robust activity within the industry to serve consumers. If a regulator ensures an industry is safe, but the industry can no longer meet the needs of or serve consumers, the regulator has likely not achieved its primary objective.

RESPONSE TO WRITTEN QUESTION OF SENATOR COTTON FROM ED TEMPLETON

Q.1. As far as you are aware, to what extent (or lack thereof) has CFPB exercised its exemption authority under Section 1022 of Dodd-Frank? Is this concerning given the broad scope and lengthy detail of some of its rulemakings, which, while not aimed at small financial institutions, can substantially and negatively impact those businesses?

A.1. The CFPB has used this authority sparingly, and many times when it has been used it has not been implemented in a way that provides a meaningful exemption. An area where the CFPB could be the most helpful to credit unions would be to use its legal authority to exempt all credit unions from various rulemakings. Given the unique member-owner nature of credit unions and the fact that credit unions did not participate in many of the questionable practices that led to the financial crisis and the creation of the CFPB, subjecting credit unions to rules aimed at large bad actors only hampers their ability to serve their members. While the rules

of the CFPB may be well-intentioned, many credit unions do not have the economies of scale that large for-profit institutions have and may opt to end a product line or service rather than face the hurdles of complying with new regulation. This is concerning, as the CFPB has the ability to address this through the exemption authority, but has not gone far enough in doing so. While the CFPB has taken steps, such as their small creditor exemption, we believe they should do more, such as using this authority to exempt all credit unions on certain rules.

RESPONSE TO WRITTEN QUESTIONS OF SENATOR BROWN FROM MICHAEL D. CALHOUN

Q.1. At the Banking Committee's February 10, 2015 hearing on regulatory relief, the OCC and FDIC proposed an increase from $500 million to $750 million the asset-size threshold that determines whether a community bank can qualify for an examination every 18 months, rather than every 12 months. What do you think about this proposal?

A.1. The Center for Responsible Lending supports allowing well-managed banking institutions with up to $750 million in assets the opportunity to qualify for an 18-month examination schedule. The result should relieve compliance costs for 300 community banks, while giving financial regulators more resources to address those institutions that present consumer protection, capital, or other issues of concern.

Q.2. At Tuesday's hearing, NCUA stated that its top priority was to obtain authority from Congress to examine third-party vendors. In addition to its arguments that it would reduce burdens for credit unions, it made the case that this authority is vitally important to protect the smallest credit unions from cyber-attacks. What are your views on this proposal?

A.2. We support NCUA's proposal to obtain authority to examine and regulate third-party vendors, including CUSOs and subsidiaries of credit unions. As noted by NCUA, this authority is given to other financial regulators, and it is an important component of supervision for both safety and soundness and consumer protection.

Q.3. As the Committee considers proposals to provide regulatory relief to community banks and small credit unions, I am reminded of an exchange that I had with then Fed Chairman, Bernanke, in July 2013. At that hearing he indicated that regulators should "do whatever we need to do to make sure the U.S. financial system is safe." Do you agree that this is the regulators' primary objective?

A.3. Given the consequences of an unstable financial system, it is clear that consumers, financial institutions, our economy, and taxpayers benefit when financial regulators prioritize the safety and soundness of the system. Yet, that priority still must be balanced with an understanding that the purpose of the financial system is to responsibly provide access to credit and capital. Each of these priorities should be equally key considerations that guide regulatory actions.

RESPONSE TO WRITTEN QUESTION OF SENATOR VITTER FROM MICHAEL D. CALHOUN

Q.1. Mr. Calhoun, in a statement on June 24, 2014, on your organization's Web site you were quoted as saying, "Despite what critics claim, Operation Chokepoint is a critical program that protects American businesses and consumers."

Please explain how attempting to cutoff lawful businesses' ability to bank in anyway protects American businesses and consumers? Do you agree with the FDIC's recent directive stating, "institutions to take a risk-based approach in assessing individual customer relationships rather than declining to provide banking services to entire categories of customers?"

A.1. The Operation Choke Point program is designed to target sources of illegal financial activity. By doing so, it ensures that our Nation's biggest banks are not complicit in activities like fraudulent debt collection, drug trafficking, and funding terrorism.

Several settlements under the program demonstrate its importance in ensuring that our bank and payment systems are not used to further illegal activities. Many of these cases addressed illegal transaction and consumer scams, such as the systematic charging of fraudulent withdrawals from consumers' accounts.

Regulators have asked financial institutions to exercise due diligence and implement appropriate controls to ensure that they are not aiding the commission of crimes. That approach is reasonable, necessary, and consistent with the FDIC's most recent directive related to the program.

RESPONSE TO WRITTEN QUESTION OF SENATOR MENENDEZ FROM MICHAEL D. CALHOUN

Q.1. Mr. Blanton's testimony calls for deeming any mortgage made by a depository institution and held in the lender's portfolio—regardless of the institution's size—to be a "Qualified Mortgage" under the Dodd-Frank Act. Meaning, a lender would be exempt from requirements to make a good faith attempt to verify a borrower's ability to repay the loan, even if the loan includes risky or exotic features or charges very high fees that might make the loan profitable to the lender even if the borrower is not able to repay it.

It's one thing to consider, as the CFPB does, whether a loan is held in portfolio as one factor among many for certain specific, targeted exemptions for small institutions. But it's another to call for making this the only factor to create an exemption for institutions of any size and loans of any type.

Mr. Calhoun, can you explain some of the problems with this approach? Didn't Washington Mutual and Countrywide, two large institutions that failed spectacularly during the financial crisis, hold mortgage loans in their portfolio of a type that would be problematic to exempt from the ability-to-repay rules?

A.1. We have serious concerns regarding this proposal. It is important to remember that, during the crisis, institutions like WaMu and Wachovia originated many unsustainable loans that they retained in their portfolios.

The reality is that lenders who maintain loans in portfolio may still pay insufficient attention to a borrower's ability to repay. This is especially true in cases where the loan creditor can earn sufficiently high up-front compensation, where borrowers have substantial equity that would cover any default risk, and where the incentives of the individual loan originators and the creditor differ.

The Center for Responsible Lending supports a narrowly tailored exemption that allows the portfolio loans of community banks, with certain characteristics that ensure ability to repay, to be treated as qualified mortgages. For example, there are important protections in the CFPB rule for small mortgage lenders and the recent proposed revisions to this rule. It maintains protections against negative amortization loans, retains limits on points and fees and ties safe harbor status to the loan having a reasonable interest rate.

In addition, it is extremely important to limit this rule to small depository institutions. Permitting lightly supervised nondepository lenders to be covered by the same rule would encourage and insulate risky lending by the very same entities that drove irresponsible lending during the housing crisis. The rule should also be limited to traditional, small banks because the community-bank-lending model is much more personalized and differs significantly from the mortgage-lending model adopted by larger financial institutions.

RESPONSE TO WRITTEN QUESTION OF SENATOR COTTON FROM MICHAEL D. CALHOUN

Q.1. As far as you are aware, to what extent (or lack thereof) has CFPB exercised its exemption authority under Section 1022 of Dodd-Frank? Is this concerning given the broad scope and lengthy detail of some of its rulemakings, which, while not aimed at small financial institutions, can substantially and negatively impact those businesses?

A.1. The Consumer Financial Protection Bureau has used a number of provisions of Dodd-Frank to tailor rules that accommodate the business differences of community banks, while also protecting consumers.

More recently, the CFPB requested comment on whether to increase the 500 first-lien mortgage cap under QM's small-creditor definition. CRL expressed support for a reasonable increase of the 500 loan cap, limiting any potential increase to rural banks or for loans held in portfolio. The CFPB's proposal quadruples the limit, expanding the loan origination cap for small lenders from 500 first-lien mortgages to 2,000. This 2,000 limit is exclusive of loans held in portfolio by both the creditor and its affiliates. The CFPB has also proposed to only include first-lien mortgage originations of small lender affiliate assets toward the current $2 billion asset cap. And, to accommodate concerns that the definition of a "rural and underserved" area is too narrow, the CFPB has proposed expanding the definition of rural areas by including census blocks as defined by the Census Bureau. Finally, the CFPB is also proposing to allow grace and qualifying periods for small creditors to adjust to current and proposed standards.

In addition to the CFPB's rulemaking exceptions, Dodd-Frank contains a number of provisions designed to ensure that CFPB regulations and activities do not negatively impact the business model of smaller financial institutions. As an example, Dodd-Frank exempts community banks from examination and enforcement actions by the CFPB; the law also requires the CFPB to go through the SBREFA rulemaking process. As a result, small businesses have the ability to comment on the Bureau's rules at an early stage and have advance notice of a rules direction. By comparison, only two other Federal agencies have to go through the SBREFA process. Finally, the CFPB voluntarily created a community bank advisory board to give institutions the opportunity to have an ongoing dialogue with the Bureau to discuss its activities.

ADDITIONAL MATERIAL SUPPLIED FOR THE RECORD

Appraisal Institute®
Professionals Providing Real Estate Solutions

February 17, 2015

The Honorable Richard Shelby
Chairman
U.S. Senate Committee on Banking, Housing & Urban Affairs
304 Russell Senate Office Building
Washington, DC 20510

The Honorable Sherrod Brown
Ranking Member
U.S. Senate Committee on Banking, Housing & Urban Affairs
713 Hart Senate Office Building
Washington, DC 20510

Dear Chairman Shelby and Ranking Member Brown:

On behalf of the nearly 22,000 members of the largest professional organization of real property appraisers, thank you for the opportunity to submit testimony relating to the hearing entitled, "Regulatory Relief for Community Banks and Credit Unions." We applaud your Committee for reviewing burdensome regulations, and offer the following comments, as real estate appraisal is one of the most heavily regulated professions in the United States.

De minimis Appraisal Threshold

The Committee received testimony about the availability of appraisers in certain rural real estate markets, and a question was asked of the federal financial institution examining agencies about the current appraisal requirement threshold, which currently stands at $250,000 for residential loans and $1 million for commercial real estate. The witness from the Federal Reserve indicated that the agencies had the appraisal threshold under review. Under Title XI of the Financial Institutions Reform and Recovery Act of 1989 (FIRREA), the agencies have the ability to maintain the appraisal threshold. In the early 1990s, the threshold initially was proposed to be set at $50,000, increased to $100,000 in a proposed rule, and raised dramatically to the $250,000 level, where it has remained since 1994.

Several facts related to the current "de minimis" appraisal threshold should be pointed out, as follows:

1. Banks are not required to obtain an appraisal for any loan below the *de minimis* appraisal threshold, which means that the current $250,000 residential threshold exempts a majority of all residential real estate loans in the United States. According to the Federal Housing Finance Agency, the current House Price Index stands at $220,000[1]. Accordingly, the vast majority of rural residential real estate loans already fall well below the current appraisal requirement.
2. Loans backed by government agencies and government-sponsored enterprises also are exempt from the appraisal requirements, which means that loans insured by the Federal Housing Administration have their own appraisal requirements, and loans bought by Fannie Mae and Freddie Mac are determined by the agencies themselves. By statute, the FHA maintains an appraisal requirement for all loans largely because of the risks associated with the FHA insurance fund, while the government-sponsored enterprises generally require appraisals for purchase-mortgage situations.
3. The period leading up to the 2008 financial crisis saw Fannie Mae and Freddie Mac reduce their appraisal requirements over time, gradually incorporating allowances for "drive-by" appraisals and automated valuation models on a high percentage of loans purchased. This ultimately proved to be a mistake, as illustrated in part by the rampant collateral valuation failures at both agencies. Since the crisis, Fannie Mae and Freddie Mac generally have adhered to an underlying appraisal

[1] See http://www.fhfa.gov/Media/PublicAffairs/PublicAffairsDocuments/MonthlyHPINovember012215.pdf

requirement, we believe, for sound reasons. Fannie Mae and Freddie Mac have also recently released FAQs related to rural appraisal concerns, dispelling several myths that permeate the banking community about GSE Seller/Servicing guideline requirements relating to comparable sales and other appraisal considerations[2]. We believe understanding around these myths can be addressed through enhanced banker education.

4. The Dodd-Frank Act established additional appraisal requirements in certain situations for banks, including a second appraisal requirement in "higher priced" mortgages, or subprime loans, and full interior inspection appraisals for property "flipping" situations. The Consumer Financial Protection Bureau has established several exemptions to these requirements in final rules published last year, but it is worth noting that these requirements are different than those established under Title XI of FIRREA. The Dodd Frank appraisal requirements are minor and very limited in scope, impacting less than 5 percent of all loans in the United States by our estimates.
5. Lastly, our review of failed banks resulting from the financial crisis, including many community banks, indicates that the vast majority had problems adhering to basic appraisal requirements, despite citations from federal bank regulatory agencies. According to our research, more than two-thirds of failed community banks previously had been cited for appraisal violations by bank regulators for such misdeeds as failing to obtain current appraisals or perform adequate appraisal reviews; relying on stale appraisals; inadequate controls of the lending function, including appraisals; and poorly explained upward adjustments to the appraisal values.

Availability of Appraisers

While the Appraisal Institute appreciates community bank concerns about the availability of appraisers in some rural parts of the United States, we strongly caution against tailoring a national policy around one particular market condition. Any one real estate market may experience rapid growth, but that growth actually may *increase* the importance of appraisals, as real estate is prone to market cycles, helping to avoid boom and bust cycles.

We see no evidence of a national shortage of appraisers. We are attaching a copy of the most recent copy of the U.S. Appraiser Population estimates, which illustrate that the total population of certified and licensed real estate appraisers stands at around 80,000 nationwide[3]. We note that the markets for residential appraisers and commercial real estate appraisals are vastly different, with the number of residential real estate appraisers declining at a rate commensurate with the decline in the residential real estate market, while the commercial real estate market has remained relatively steady, even increasing in recent years. Recent declines in the ranks of residential appraisers actually indicate an *oversupply* of residential appraisers, if anything. We urge the Committee to consider the differences between residential and commercial real estate before taking legislative action to fully assess problems and solutions. To this point, it is unclear to us from the testimony whether community banks were facing difficulty with residential appraisals or commercial appraisals or both.

Collateral Underwriter

Fannie Mae recently announced the availability of a new program for mortgage loan sellers to conduct an electronic quality control assessment of appraisals. "Collateral Underwriter" utilizes data collected from previous appraisals prepared on loans sold to Fannie Mae and other analytics to score appraisals via a risk rating system. Scores of 4 or 5 are viewed by the system as carrying higher collateral risk, with scores of 1 or 2 illustrating less collateral risk, according to the system. The scores are not a rating of the *appraiser*, but of the *appraisals* as they relate to data maintained by Fannie Mae.

The release of Collateral Underwriter has widespread effects on the mortgage lending process and accompanying analytical processes. Collateral Underwriter is borne out of the idea that Fannie Mae's pre-

---

[2] See https://www.fanniemae.com/content/faq/appraisal-property-report-faqs.pdf
[3] See http://www.appraisalinstitute.org/assets/1/7/us-appraiser-demographics_(1).pdf

2008 crisis appraisal policies failed, a point that cannot be disputed. Clearly, outsourcing all appraisal review responsibilities to mortgage loan sellers was a mistake. To be clear, Fannie Mae never even saw appraisals prepared for loans that it bought unless the loan went into foreclosure. On this point, we strongly support efforts to conduct more due diligence on appraisals ***prior to*** purchasing loans, which programs like Collateral Underwriter attempt to do.

Quality assurance tools have been on the market for many years, but Collateral Underwriter is different in that the databases that support the tool are larger than any proprietary system and the program is delivered by the largest loan purchaser in the market. We note that the program accompanies assurances by the Federal Housing Finance Agency to address repurchase relief, so we believe that while the program is voluntary, many loan sellers will pay close attention to what Collateral Underwriter says to gain cover from repurchase risk.

This carries with it many questions and concerns about unintended effects on mortgage lending, real estate appraisal and, ultimately, systemic risk. Some context is necessary. Leading up to the 2008 financial crisis, the Fannie Mae and Freddie Mac seller/servicing guidelines also were viewed only as "guidelines," but they gradually became viewed by mortgage participants as "rules" that must be followed. We do not believe that such rules-based approaches produce more credible appraisals, and actually may increase collateral risk, especially if developed and maintained in a vacuum.

Similarly, we are concerned that Collateral Underwriter messages and alerts will be viewed by mortgage loan sellers as rules for appraisal reviewers to follow. Such a development could jeopardize the independence of the appraisal process and create a systemic risk, as the system potentially becomes self-fulfilling.

Part of our concern here is the continued allowance of mortgage loan sellers to use underwriters and others with marginal appraisal review qualifications to manage appraisal review processes. Generally, our members report having less difficulty with treating quality assessment tools such as Collateral Underwriter like a rules-set where qualified reviewers are in place. This is because qualified reviewers can spot trivial concerns and focus on meaningful alerts that have bearing on the quality of the appraisal. Many times these issues are addressed in narrative comments by the appraiser, but this requires that someone actually read and thoroughly review the appraisal. This stands in contrast to many situations today where underwriters and others simply request that appraisers "clear" or "override" Collateral Underwriter alerts, which appraisers cannot do.

Lenders in rural areas have reason to be concerned about rules-based approaches, because such rules generally do not work well in non-conforming markets. We already are hearing that some loan sellers may not fund loans that have appraisals with high Collateral Underwriter risk ratings of 4 or 5, even though appraisals with such risk ratings actually may be well supported and credible, but just vary from Fannie Mae's databases (which may contain incorrect information). On the other hand, appraisals with risk scores of 1 or 2 may conform to Collateral Underwriter rule-sets, but may not be well-supported or credible when scrutinized by a qualified reviewer.

To its credit, Fannie Mae has attempted to dispel some of these concerns in a Lender Letter released earlier this month[4]. The Letter does a commendable job of addressing concerns about the standing of Collateral Underwriter in the market and use by mortgage loan sellers. Still, our fears about Collateral Underwriter being viewed as a set of rules remain given past experiences with guidelines implemented by mortgage loan sellers. We encourage the Committee to review this development to ensure that Collateral Underwriter is not treated like a set of rules by mortgage loan sellers and that no systemic risks are

[4] See https://www.fanniemae.com/content/announcement/ll1502.pdf

created. Further, we encourage the Committee to examine whether Fannie Mae's appraisal review policies, in light of housing finance reform, ensure that credible reviews take place.

Evaluations

Though appraisals are not required for loans of $250,000 or less, under federal bank regulatory policy, lenders must obtain an "evaluation" to understand the collateral risk involved with the loan. Many evaluations are completed by staff of financial institutions, but many also are outsourced to third parties such as real estate brokers, who often prepare broker price opinions to assist a bank in the creation of an evaluation. We believe that appraisers are the best source for all valuation services, including evaluations; however, the current regulatory regime imposed by FIRREA makes this very difficult because of certain requirements found in the Uniform Standards of Professional Appraisal Practice. USPAP appraisals are required above the *de minimis* threshold, but there is nothing to prohibit an appraiser from providing "evaluation" services, except that USPAP creates certain competitive disadvantages to appraisers in this space. For instance, unlike any real estate broker preparing a broker price opinion, appraisers are required to maintain certain record keeping requirements related to any valuation service, including evaluations. Advisory Opinion 13 in USPAP indicates the following regarding evaluations:

> *"An evaluation, when performed by an individual acting as an appraiser, is an appraisal. In addition to complying with USPAP, the appraiser must be aware of and comply with any additional assignment conditions and reporting requirements imposed on the assignment."*

In other words, USPAP prohibits a licensed or certified appraiser from preparing an evaluation without also complying with USPAP.

We are supportive of states enacting laws that give appraisers greater flexibility for the standards under which they are preparing valuation services, as there are several generally recognized standards available to U.S. appraisers today. However, we believe that appraisers would benefit from a clear and explicit exemption from USPAP wherever an appraisal exemption is allowed. We believe this would service users of appraisal services well, as it would enable them to obtain cost-competitive valuation services from the most qualified sources in the market.

We note that this issue was addressed in a bill that was considered in the House last session. H.R. 5148, the "Access to Affordable Mortgages Act of 2014," which passed the House Financial Services Committee in the last Congress, granted an exemption from conducting appraisals in accordance with the USPAP for certain "high risk mortgage loans." H.R. 5148 creates flexibility for lenders to turn to appraisers to provide cost-competitive valuation services.

Unauthorized Activities

We need to make real estate appraisal an attractive profession for younger generations to explore and pursue. This is ultimately the best way to avoid a shortage in the future of highly qualified valuation experts. While appraisals should be prepared in accordance with minimum standards related to things like ethics and competency, great pains should be taken to avoid the appraisal practice (methods and techniques) from being dictated by rules and regulations. Appraisal methods and techniques, or generally, the three approaches to value (the sales comparison, cost and income capitalization approaches), should be left to the judgment of appraisers. This is one of the things that makes real estate appraisal attractive as a profession – it's an applied science. Our experience with nearly 100 years as a profession indicates that there is an exception to every rule in real estate, and that's because the real estate market in the United States is so diverse. Methods and techniques that work in a homogenous neighborhood in Washington, DC, may not work in the rural upper Midwest, which illustrates the importance of professional judgment on the part of an appraiser.

Testimony of the Appraisal Institute
Regulatory Relief for Community Banks and Credit Unions
February 17, 2015

Today, we are facing the potential for a new and unauthorized set of rules to dictate the appraisal process. The Appraisal Foundation, a private nonprofit organization that was authorized by Congress under Title XI of FIRREA to promulgate USPAP and establish minimum licensing requirements for appraisers, recently established a third board called the "Appraisal Practices Board." The creation of this board was undertaken under suspect circumstances, about which we previously have testified to Congress. Despite these and other concerns about conflicts of interest created, given its existing authorizations from Congress, the Appraisal Foundation continues to encourage state appraiser regulatory agencies and others to adopt works of the Appraisal Practices Board for mandatory compliance by certified and licensed appraisers. This would have strong negative effects on the appraisal process and impose new liabilities and regulatory burdens on appraisers and users of appraisal services. We believe it places the entire profession in jeopardy.

We encourage any effort by the Committee to promote regulatory relief to consider including and enacting regulatory relief measures for appraisers, including limitations around the authority of the Appraisal Foundation in the areas of appraisal practice in light of the existing authorizes bestowed by Congress. .

Thank you for the opportunity to speak on the record, and we will be happy to answer any questions you might have.

Sincerely,

Appraisal Institute